



Department of Political and Social Sciences

**Choosing Lesser Evils:
The Role of Business in the Development of the
German Welfare State from the 1880s to the
1990s**

Thomas Paster

Thesis submitted for assessment with a view to obtaining the degree of
Doctor of Political and Social Sciences of the European University Institute

Florence, June 2009

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Abstract

This thesis is an empirical study of the role of organized business in the formation of market-correcting industrial relations and welfare state institutions, relying on a historical-diachronic case study of welfare state development in Germany from the 1880s to the 1990s. How did the formation of the “German model” become possible in the face of employers’ structural power? The thesis confronts two alternative theoretical perspectives for explaining employers’ acceptance of market-correcting institutions: an *economic-functionalist explanation* (“cross-class coalition thesis”) and a *political-strategic explanation* (“political accommodation thesis”). The first one focuses on economic benefits derived by specific types of firms from welfare state and industrial relations institutions, the second on political constraints and changes in the political power structure, and employers’ strategic responses to them. The thesis finds that the political accommodation thesis has greater explanatory power and challenges business interest-based explanations of welfare state development.

The empirical analysis in the thesis traces the preferences (interest perceptions), strategic considerations, and resulting policy positions of the national employer federations in Germany during three different political regimes: the Wilhelmine Empire (1871-1918), the inter-war Weimar Republic (1918-1933), and the post-war Federal Republic (1949-1990s). The analysis focuses on those historical reform events that, in retrospect, came to shape welfare state and industrial relations institutions in Germany. Process analysis based on historical sources and diachronic comparison are used as methods to reconstruct (i) the motivations of employers for supporting or opposing specific policy options, and (ii) the socio-political and institutional environment within which employers formed their preferences and strategies. The thesis uses Germany as a *crucial case study* because of the paradigmatic character of this country as a type of non-liberal capitalism that is often understood to benefit certain types of firms today.

Empirically, the thesis finds that employers tended to play a constraining role in the development of industrial relations and welfare state institutions and often accepted specific reform options for political-strategic reasons, rather than because of any perceived economic interests in them. The thesis identifies two dominant employer strategies in welfare state politics (a) *pacification* of radicalized elements within labor, and (b) *containment* of expansionary reform projects. Moreover, the thesis finds that employers consistently preferred conservative types of social policies to universalist (social democratic) alternatives, and explains this as a result of differential impacts on work incentives. The deliberate formation of cross-class coalitions is found to have been rare and to have happened only under conditions of extraordinary political and economic uncertainty. Issues of skill formation are found to have played a marginal role.

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List of Abbreviations

ACC	Allied Control Council
ADGB	Allgemeiner Deutscher Gewerkschaftsbund (General German Federation of Labor Unions)
AEG	Allgemeine Elektrizitätsgesellschaft (General Electric Company)
AVAVG	Federal Law re. unemployment insurance and employment services (1927)
BDA	Bundesvereinigung Deutscher Arbeitgeberverbände (Federation of German Employer Associations)
BdI	Bund der Industrie (Federation of Industry, 1895-1919)
BDI	Bundesverband Deutscher Industrie (Federation of German Industry)
CDI	Centralverband Deutscher Industrieller (Central Association of German Industrialists, 1876-1919)
CDU	Christlich Demokratische Union (Christian Democratic Party)
CSU	Christlich Soziale Union (Christian Social Party)
DAF	Deutsche Arbeitsfront (German Labor Front, NS organization)
DAGZ	Deutsche Arbeitgeberzeitung (an employer periodical)
DGB	Deutscher Gewerkschaftsbund (German Federation of Labor Unions)
DIHT	Deutscher Industrie- und Handelskammertag (German Diet of Industry and Commerce)
DM	Deutsche Mark (currency)
DNVP	Deutsch-Nationale Volkspartei (German National Peoples' Party)
DVP	Deutsche Volkspartei (German Peoples' Party)
ECSC	European Community for Coal and Steel
FDI	Foreign Direct Investments
FDP	Freie Demokratische Partei (Free Democratic Party)
FRG	Federal Republic of Germany
GDR	German Democratic Republic
GHH	Gutehoffnungshütte (iron and steel works company)
HDG	Hilfsdienstgesetz (War Auxiliary Services Law, 1916-1918)
IGM	Industriegewerkschaft Metall (German Metalworker Union)
IHK	Industrie- und Handelskammern (Chambers of Industry and Commerce)
INSM	Initiative 'New Social Market Economy'
MAN	Maschinenfabrik Augsburg-Nürnberg (machinebuilding company)
NGISC	North German Iron and Steel Control (Allied authority)
NLP	National-Liberale Partei (National Liberal Party)
OT	Ohne Tarifbindung (without collective bargaining obligation)
RDI	Reichsverband Deutscher Industrieller (National Federation of German Industry, 1919 – 1934)

SPD	Sozialdemokratische Partei Deutschlands (Social Democratic Party)
USDP	Unabhängige Sozialdemokratische Partei (Independent Social Democrats)
VDA	Vereinigung Deutscher Arbeitgebervereine (Federation of German Employer Associations)
VDESI	Vereinigung Deutscher Eisen und Stahlindustrieller (Association of German Iron and Steel Industrialists)
VSME	Verband der Sächsischen Metall- und Elektroindustrie (Association of the Saxon Metal and Electrotechnic Industry)
VoC	Varieties of Capitalism approach
ZAG	Zentralarbeitsgemeinschaft (‘Central Working Committee’)
ZDH	Zentralverband Deutsches Handwerk (Federation of the German Craft)

1 Introduction

In capitalist societies, business has structural power due to its control over production and investments on which societal prosperity depends. Given this structurally privileged position of business, how did capitalist societies manage to establish policies and institutions that constrain entrepreneurial freedom and impose high costs on firms, such as welfare state programmes? Conventionally, the uneasy coexistence of a capitalist economy and welfare state institutions has been explained in the comparative political economy literature as the product of a social compromise that resulted from class conflicts and the political power resources of labor. Michael Shalev, for instance, argued that “the welfare state is a class issue. Logically and historically, its principal proponents and defenders are movements of the working class” (Shalev 1983: 319). In a similar way, Huber and Stephens argued that the “struggle over welfare states is a struggle over distribution, and thus the organizational power of those standing to benefit from redistribution, the working and lower middle classes, is crucial” (Huber and Stephens 2001: 17) development (for general overviews of different theories of welfare state development see Hicks and Esping-Andersen 2005; van Kersbergen and Manow 2008; and Huber and Stephens 2005: 552-5).

More recently, from the 1990s onwards, this perspective has been challenged by a new theoretical perspective that intends to “bring capital back in” (Swenson 1991) to the analysis of welfare states and political economies. As Kathleen Thelen has remarked, the earlier focus on the political role of organized labor and its political allies has “by and large been replaced by a concern with uncovering the role that employers have played in generating and sustaining such institutions” (2002: 380). This strand of research focuses on the interests and preferences of business, rather than labor, for explaining welfare state development, trying to provide a so-called *employer-centred explanation* for the historical formation and expansion of modern welfare states.

Inspired by a specific type of economic functionalism, employer-centred explanations often assume that employers held a genuine economic interest in the formation of welfare state programmes and other market-correcting institutions. According to this perspective, benefits in terms of economic competitiveness or economic productivity motivated specific types of firms to back welfare state formation. These interest perceptions led to a congruence of policy preferences between parts of capital and parts of labor and to the formation of cross-

class alliances. According to this view, cross-class alliances are the political foundations on which welfare state formation rests (Mares 2003a, 2003b; Swenson 1991, 2002). I refer to this new argument as the “*cross-class coalition thesis*”. This argument – if correct - puts into question the traditional “power resource” explanation of welfare state development, which highlights the importance of class struggle and the political power resources of the labor movement and its political allies. It challenges the centrality of labor strength as an explanatory variable of welfare state development by highlighting the importance of business interest in the process of welfare state-making.

At the center of the cross-class coalition approach are three closely related claims: (a) employers (or dominant groups among them) had actively supported the construction of modern welfare states; (b) they had done so because they had genuine economic interests in welfare state policies, as these policies benefited their modes of industrial production; and (c) a convergence in the preferences of capital and labor resulted in the formation of cross-class alliances. According to this argument, cross-class alliances are the political settlement on which the institutions of the modern welfare state rest. Major labor market and social policies have been constructed not as policies *against employers*, but instead as policies *supporting* employer interests (for a general introduction to the debate see Thelen 2002: 377-82). If this new employer-centred explanation of welfare state development is correct, traditional labor-centred explanations need to be reconsidered. Peter Swenson points out that if employer interests regarding social policy are strikingly more positive where labor is strong, than the “political power of labor...is indeed spurious if conceived exclusively as ‘power against capital and its interests’” (Swenson 2002: 10).

The subject of this thesis is the evaluation of employers’ contribution to welfare state development in light of this controversy, relying on an in-depth analysis of the German case. The basic research questions that this thesis tries to answer are the following: *What was the role of industrial employers in the construction of the German welfare state?* To what extent and under what conditions did employers accept or endorse reforms introducing or extending welfare state and industrial relations institutions? What motivated their decisions to support or oppose specific reform projects?

The argument made in this thesis highlights the importance of political conflict and strategic adaptation for motivating employers to accept specific welfare state policies, and, by doing so, takes issue with existing employer-centred explanations. The thesis tries to show that employers accepted the introduction of specific welfare state programmes and industrial

relations institutions as *lesser evils*, where the maintenance of unregulated markets became politically unviable, rather than because they thought that these policies would benefit the competitiveness or productivity of their firms. A positive association between the social policy stances of business and labor power may indicate that labor power is a spurious variable, as Swenson plausibly suggests, but it may also indicate, I suggest, that employers adjusted their positions in response to labor strength or other constraints coming from the political context. The argument presented in this thesis thus pulls us back to the importance of political conflict and balance of power, emphasized by the traditional “power resource” explanations.

To preview the main argument of the thesis, I argue that employers’ had no genuine economic interests in the introduction of welfare state programmes and institutions of class compromise but were, nevertheless, sometimes compelled by political constraints to support their introduction. Their motivations for accepting or endorsing specific policies and institutions have been twofold: First, employers accepted or supported specific reforms to contain the rise of the labor movement or radical elements within it. Employers used social policies and institutions for class compromise as tools of social pacification. Social policies were the lesser evil compared to revolution and collectivization of industry. When the revolutionary dangers waned, employers’ interest in pacification waned as well. Second, employers tried to limit the scope and generosity of welfare state programmes by what I call the *politics of containment*. In order to prevent far-reaching reform plans from implementation, they endorsed and supported more moderate alternatives. In both cases, containing political challenges motivated employers to go along with welfare state reformers. The formation of the modern welfare state was not relentlessly opposed by industrialists, but it is unlikely they would have accepted it in the absence of formidable political challenges.

On a theoretical level, the thesis challenges a specific type of economic-functionalist thinking in political economy that assumes that the behavior of political actors can be inferred directly from their stipulated material interests. Political actors are embedded in a specific historical political context and this context shapes their goals and positions. Their policy stances are not determined by their objective material interests alone. They are also, in part, the result of strategic considerations, the result of an accommodation to political constraints. They are calculations of what is the best that can be achieved in a given context. If their best option is politically unviable, employers may, for instance, support the policy that is their second-best option in order to prevent implementation of a different option that they consider

to be even worse. In this case their position does not reflect a genuine or *first-order* preference but an accommodation to the political context.

An analysis of the role of employers in welfare state development, I suggest, needs to take into account how employers accommodate to the political context they are embedded in, in order to understand their true causal relevance for welfare state development. Before turning to the question of how political context shapes employer preferences and strategies, the following section reviews the key arguments in the controversy over employers' role in welfare state development in more detail.

1.1 Theory: Class Alliances and Class Conflicts in Political Context

Much of the recently thriving literature on the role of employers in welfare state development emphasizes the supportive role of employers in welfare state development and their pivotal role in the formation of so called "cross-class alliances". The emphasis on the importance of political alliances among social groups is not distinctive of the cross-class coalition approach or of employer-centred explanations. As one political group usually does not possess sufficient power to implement a desired political goal without the support from other groups, the formation of alliances is a pervasive phenomenon in politics. What makes the cross-class coalition approach distinctive and innovative, however, is the claim that the political alliances that shaped welfare state development brought together segments of capital and labor, that is, the claim that political alliances in welfare state development bridge the class divide, rather than following it.

In the comparative and historical analysis of welfare state development, the formation of alliances between different social groups has been emphasized as an important factor by several scholars, but, unlike in the cross-class coalition approach, these scholars did not emphasize alliances that include employers as pivotal actors, but instead alliances forged by the working class with other social groups. The distinctive element of the cross-class coalition approach, as understood here, is that it claims the importance of *employer-centred alliances*. This section will first discuss some important examples of the study of political alliances in welfare state development and political economy more generally and show how theoretical arguments made in some of these studies have inspired the cross-class coalition thesis. The second part of the section analyzes the core arguments made by proponents of the cross-class coalition thesis and employer-centred explanations in more detail.

Precursors to the cross-class coalition approach

Barrington Moore's analysis of the transitions from feudalism to industrial society in *Social Origins of Dictatorship and Democracy* emphasizes the importance of alliances and conflicts between different social classes in explaining different pathways to industrial modernity (Moore 1966). Moore identifies "three main historical routes from the preindustrial to the modern world" (Moore 1966: xii), which differ in the social forces and their relations to each other that have underpinned this transition. Moore tries to understand, in particular, "the role of the landed upper classes and the peasants in the bourgeois revolutions leading to capitalist democracy, the abortive bourgeois revolutions leading to fascism, and the peasant revolutions leading to communism" (Moore 1966: xiv). To put it simply, Moore argues that different configurations of alliances and cleavages between large social forces are the most important factor explaining differences in the outcomes of historical regime transformations. His work constitutes a seminal example of the empirical analysis of class cleavages and alliances.

In the field of welfare state research, Esping-Andersen's *Politics against Markets* has pointed out the important role of class alliances. Unlike the cross-class coalition approach, as understood here, his analysis does, however, not focus on alliances involving employers, but on electoral alliances forged by social democratic reformers aiming to sustain popular support for their welfare state projects. According to Esping-Andersen, social democratic reformers in Denmark and Sweden constructed universal social policies with the intention of "supplanting narrow group identities or individualism with broad social solidarity" (Esping-Andersen 1985: 33). He argues that the success of Scandinavian social democrats in constructing a generous and comprehensive welfare state cannot be explained solely by the strength of the social democratic labor movement, but by its exceptional ability to forge alliances with other social classes.¹ Social democratic parties "conceived as strictly working-class movements, are and always have been, doomed to fail." Instead, social democratic power "depends on a combination of two historical forces: the pattern of class coalitions and the party's conduct of class mobilization through reformist practice" (Esping-Andersen 1985: xv).

Esping-Andersen argues that Nordic social democracy has been more successful in engineering such class alliances than their continental European counterparts, which explains differences in character and generosity between Nordic and continental European welfare state regimes. He identifies two types of class alliances: in the first half of the 20th century, a

¹ A similar argument is made by Adam Przeworski, who stresses the "electoral dilemma" between maintaining a homogenous class base and struggles for electoral success (Przeworski 1985: 102).

popular alliance between peasants and industrial blue-collar workers (“red-green alliance”) led to the introduction of egalitarian, universal social citizenship policies. During the post-war decades an alliance between industrial blue-collar workers and white-collar workers (“wage-earner alliance”) was responsible for the construction of earnings-related social insurance policies. As mentioned, employers do *not* figure as pivotal actors, either in the first or in the second type of alliance. Esping-Andersen’s analysis constitutes a modified version of, rather than a fundamental departure from, the labor mobilization thesis. The pivotal actors are reformist social democrats trying to engineer popular support for their policies (Esping-Andersen 1990: 17-8).

A related argument is made by Peter Baldwin (1990). Baldwin challenges the labor mobilization thesis by arguing that it neglects the role of the middle classes. Through historical analysis of important reform projects in Denmark, Sweden, France, Germany and the UK, Baldwin shows that middle class groups, like white-collar employees or independent artisans, often supported social policies for self-interested reasons. They wanted social protection, but insisted on privileged treatment, better benefit conditions and earnings-related benefits in order to maintain status distinctions to lower classes. Like in Esping-Andersen’s account, industrial employers do not figure as pivotal supporters of welfare state development in Baldwin’s work.

Employers were brought into the analysis of political alliances, initially, by studies dealing with foreign economic policies and foreign trade. Peter Gourevitch’s study of foreign economic policy-making has played a seminal role in developing the notion of cross-class alliances (Gourevitch 1986, 1989). In *Politics in Hard Times*, Gourevitch’s goal is to analyze “the patterns of support which have formed around the various programs of economic policy that countries have adopted in response to severe disruptions in the international economy” (Gourevitch 1986: 20). His key assumption is that the foreign economic policy preferences of political actors will be determined by their position in the international economy: “Societal actors divide and combine over time in ways that relate to their changing situations in the international division of labor” (Gourevitch 1986: 32). The basic policy choices at stake are free trade vs. protectionism, whereby different social groups are likely to benefit from either the former, or the latter, depending on the international economic context.

Gourevitch makes the observation that different sectors of the economy are positioned differently in the international economy, which he makes the basis for an analysis of political alliances that stresses *cross-sectoral cleavages*, rather than cross-class cleavages. Gourevitch

shows that on some issues industrial employers had been divided, due to the different international economic situation they faced, which in some cases led to sectoral cross-class alignments. Dynamic, competitive sectors have tended to favor free trade, sectors facing stiff international competition tended to favor protectionism. These disagreements “have been strong enough to break through common ‘class’ positions and assert ‘sectoral’ ones. At times these conflicts have led business leaders to make common cause with ‘class’ enemies (‘labor’) or sectoral ones (‘agriculture’)” (Gourevitch 1989: 97). “The move for free trade,” in particular, “was one of the prime elements leading business to seek labor allies” (Gourevitch 1989: 98). Gourevitch shows convincingly that the sectoral conflicts over the issue of free trade can motivate groups of industrial employers to forge a sectoral cross-class alliance. Although his analysis does not focus on social policy issues, concessions by industrialists on social policy issues may potentially have played a role in engineering such “free trade alliances”.

Sectoral conflicts over issues of foreign economic policy are also analyzed in the work of Jeff Frieden (Frieden 1991; Frieden 1988). Frieden assumes that economic openness and integration creates winners and losers, and therefore has distributive consequences that will matter in domestic politics. In an analysis of the US foreign economic policy during the inter-war period, Frieden shows that this policy was closely linked to conflicts of interests and, thus different preferences, between firms that saw free trade as an opportunity for expansion and firms which saw free trade as a competitive threat (Frieden 1988). In a similar way, Frieden has theoretically modeled the preferences of different producer groups concerning exchange rate policy, emphasizing that different sectors will be affected differently by international capital mobility and will thus have different preferences with respect to exchange rate policies (Frieden 1991). Neither Frieden nor Gourevitch have applied their propositions to the field of welfare state development, but, as we shall see below, the logic of their cross-sectoral cleavage arguments came to inform the theoretical basis of the cross-class coalition approach in welfare state research.

Like Frieden and Gourevitch, also Ronald Rogowski has focused on the role of the international economy in explaining domestic patterns of political cleavages and alliances. Different to Frieden and Gourevitch, however, he assumes cleavages between the factors of production rather than between sectors. Rogowski tries to explain different cleavage and alliance patterns across countries with the differential effects of exposure to international trade on different social groups. Rogowski uses a basic three factor model (land, capital and labor) and builds on the Stolper-Samuelson theorem, according to which abundant factors will

benefit from international trade, while scarce factors will lose. From this assumption he derives a model of alliance formation, which, put in simplified terms, suggests that those factors benefiting from international trade will ally against those losing from international trade. He hypothesizes that “changes in exposure to international trade” will “profoundly affect nations’ internal political cleavages” (Rogowski 1989: 20). The modeled results will be either a “red-green alliance” (land and labor vs. capital), a class alliance (labor vs. capital and land) or an “urban-rural alliance” (capital and labor vs. land) (Rogowski 1989: 4-16). To sum up, this section has shown that the notion of cross-class alliances is rooted in studies of foreign economic policy-making.

The cross-class coalition thesis: economic interests and employer politics

The notion of *cross-sectoral cleavages* of interests developed by Frieden and by Gourevitch has been applied to welfare state analysis by scholars using the cross-class coalition approach. This approach challenges the class mobilization thesis by arguing that the latter has overlooked the pro-active role of employers in welfare state development. The core argument of the cross-class coalition thesis is that employers in specific sectors had supported certain labor market and social policies because they perceived these policies to be in their own interest. This argument rests on the assumption that employers in different sectors of the economy have different interests with respect to labor market and social policies. Instead of being the outcome of class conflicts, major welfare state programmes are seen as the outcome of conflicts between different sectors of the economy. Employers in specific sectors have actively advocated labor market and social policies, usually in alliance with labor unions in the same sector, or sometimes also in a different sector. Thus, different welfare state models are seen as being as much the outcome of struggles within as between classes.

Peter Swenson is one of the most outspoken protagonists of this argument. He has analyzed the role of employer organizations in the construction of wage bargaining systems and welfare state programmes on the basis of detailed historical case studies. His studies compare Germany and Sweden (Swenson 1989), Denmark and Sweden (Swenson 1991), and the USA and Sweden (Swenson 2002). “In Sweden, as in the United States” Swenson argues

employers quietly endorsed the main components of the welfare state, not out of resignation but out of self-interest. In Sweden, the historical facts suggest, the enduring political success of the Social Democratic labor movement and the durability of its famous social and labor market policy reforms would not have been possible had they been imposed against the interests of capital (Swenson 2002: 293).

Swenson claims that employers' acceptance of major welfare state programmes reflects their genuine interest in these policies, rather than a strategic decision to accommodate to an unfavorable political context. In his view, Swedish employers had an economic interest in state regulation, because of the kind of production strategy they pursued (Swenson 2002: 12). Similarly, with regard to Germany, he argues that "because of their managerial interests—not a desire to suppress socialism—the leadership of German industry supported the building and maintenance of the world's first welfare state" (Swenson 2005: 196). Swenson, thus, rejects the argument that employers' acceptance of social policies reflects strategic or *lower-order* preferences, and insists, instead, that their positions reflect genuine or *first-order* preferences: "[T]he interests that employers expressed" in Sweden, Swenson claims:

were not ... the "strategic" preferences of a capitalist class that was, at heart, antagonistic to social and labor market legislation. Organized employers were not merely resigned to hegemonic Social Democrats and hoping to appease them for special consideration on particular details, for nicer treatment in other domains, or to avoid public disfavor. They knew what they wanted. Sometimes they liked best what they got and got what they liked best (Swenson 2002: 11).

Initially, Swenson developed his theoretical arguments about the importance of employers in welfare state development on the basis of a comparative-historical analysis of the centralization of wage bargaining in Denmark and Sweden (Swenson 1991). In this study, Swenson shows convincingly that employers in the trade-exposed metalworking sector, where wages were low, favored a centralization of wage bargaining in order to rein in the exorbitant wage growth in the construction sector, which was sheltered from international competition and characterized by militant unions. By centralizing wage bargaining, employers and labor unions in the metalworking sector intended to tame the militant construction unions and reduce the inter-sectoral wage gap (Swenson 1991: 521-523). Swenson argues that the centralization of wage bargaining in Sweden was "more the product of a cross-class, inter-factional coalition of interests than an armistice between classes at war, for there were to be losers in each camp" (Swenson 1989: 34). The integral role played by Swedish employers in centralizing wage bargaining has also been documented by other scholars, in particular in studies by James Fulcher (1991: 67-81; 190-3), Axel Hadenius (1976: 194) and Geoffrey Ingham (1974: 23; see also Crouch 1994: 107; and Scharpf 1987: 182).

Swenson, however, extends the scope of his argument by claiming that Scandinavian employers had formed a cross-class alliance with social democratic reformers to jointly

construct comprehensive welfare state programmes. He claims that the “political domination of social democrats” in Denmark and Sweden:

was stabilized by the absence of intense political opposition by capital to policies and programs aggressively opposed by business elsewhere in the world. This quiescence was not a symptom of weakness or dependency. Instead, it was a product of the class-intersecting, cross-class alliance behind institutions of centralized conflict resolution that routinely served mutual interests of sectoral groupings that dominated employer and union confederations. In *class-divisive, cross-class alliances* these groups mutually reinforced each other’s power to control intramural competitors and opponents (Swenson 1991: 514, my emphasis).

This claim goes far beyond the empirically documented pro-active role of SAF in the centralization of industrial relations in Sweden. Swenson’s analysis does, however, not present convincing empirical evidence for the claim that welfare state development in Denmark and Sweden rests on a political settlement characterized by “class-divisive, cross-class alliances.” Niklas Stenlås has shown that even during the 1940s, at the time during which Swenson’s cross-class alliance crystallized, dominant groups within Swedish industry provided substantial financial support to the Conservatives and the Liberals and their affiliated newspapers (Stenlås 1998: Ch.5 and 6). According to Stenlås, Swedish industrialists eventually “choose to cooperate with Social Democracy rather than fight it” after they had unsuccessfully spent “considerable amounts of money and resources in attempts to vie for ... [their] position and influence political ideology in Sweden” (Stenlås 1998: 363)². Organized in the so-called “Directors’ Club”, they tried to strengthen the bourgeois parties before the 1936 elections in order to prevent a Social Democratic government (s.a. Söderpalm 1976: 31-6).

Swenson acknowledges that employers had rarely been agenda-setters for welfare state reforms. Instead, they had often decided to back reforms only once the reform process had been initiated by other actors. He argues that this initial hesitation to back reforms was motivated by strategic considerations, while their final acceptance of reforms reflected their genuine interests. Referring to the New Deal reforms in the US, he argues:

[E]mployers were rarely the initiating or driving force ... There were good reasons for this de facto political division of labor ... individual capitalists had to consider the entirely avoidable business or social costs of taking progressive political stands for their relations with buyers, suppliers, stockholders, and fellow country club members when reactionary organizations set the tone of debate. Most, of course, had neither the time nor inclination to devote resources to studying the advantages or disadvantages of social legislation. ... For those businessmen with progressive tendencies ... it was probably better to lie low and wait for outside forces to push for change. The added advantage was that they could blame a *force majeure* for the reformist course of events they supported once reform was under way and justify their participation by

² A similar argument is also made by Korpi (2006).

saying that if they did not go along, worse things could happen (Swenson 2002: 13, emphasis in original).

Swenson, thus, suggests that progressive industrialists held covert sympathies for social policy reforms, but hesitated to take a clear stance because of fears of reprisals from conservative industrialists. If we assume that this is true, this argument raises the question of how progressive employers managed to have a crucial influence on the shape of the New Deal reforms, considering that they hesitated to take a clear stance. Swenson suggests that New Deal reformers paid close attention to what was acceptable to important groups of industrialists, even though these industrialists had not been outspoken advocates of the New Deal reforms. This interpretation has been challenged by other scholars. Hacker and Pierson, for instance, find that “most employers strongly opposed the enactment of a national system of social insurance” and that “only a sharp decline in business power made the SSA possible” (Hacker and Pierson 2002: 298).

A partly related argument is made by Colin Gordon. Gordon analyzes the role of business in the origins of the social policy legislation of the New Deal era in the US (ca.1933-37) (Gordon 1991, 1994). He highlights the primacy of business interests in the formulation of New Deal social policy legislation. He argues that “the New Deal was a creature of business demands” (Gordon 1994:4) and reflected the privileged position of business in the political system of the US: “Throughout the 1920s and early 1930s...U.S. welfare policy has been, in large part, a business measure in progressive clothing” (Gordon 1991:167).

Gordon relates the New Deal legislation to experiments by US firms in the 1920s with company welfare schemes and collective bargaining and the inadequacies of state-level social policies. During the 1920s many firms established company welfare schemes in order to reduce labor turnover and forestall unionization by binding worker interests to the individual firm. Due to intensifying cost competition from firms that did not have such schemes and initial underestimation of the program costs by firms, many of these “welfare capitalists” over time began to seek ways of escaping the costs associated with these programs. At the same time, a disparate patchwork of social policies at the state level had developed during the 1920s, which meant higher labor costs for firms located in “welfare” states. These happened mainly in northern states, while few southern states had established welfare programs. These private and state-level social policy innovations resulted in competitive disadvantages for firms and states with larger welfare burdens (Gordon 1991: 171-9).

According to Gordon, firms with company welfare schemes and firms in the welfarist northern states lobbied for federal welfare legislation in order to create a level playing field with regard to labor costs. These employers intended to socialize the costs of social protection and to standardize labor costs by spreading the cost burden to low cost competitors. In contrast, small firms without company welfare schemes and employers in the southern states opposed federal social policies as targeted against them. In short, Gordon argues that “federal social security was largely an effort...to “even out” the competitive disparities resulting from two decades of private and state-level experimentation with work benefits” (Gordon 1994: 4). In his view, important business groups did thus try to overcome the “competitive federalism” of the US system by deliberately pushing for nationally uniform labor standards and social policy legislation in order to mute inter-state competition. Gordon concludes that:

Federal welfare law, although a long-standing goal of academic and social reformers, was largely the product of business anxieties and demands. The SSA, of course, also counted many business opponents...By and large, however, the passage of the Act reflected a scramble for competitive or political advantage among business and regional interests. (Gordon 1994: 241)

Gordon makes a similar argument with respect to unionization and collective bargaining in the 1920s. While acknowledging that most US industries were strictly anti-unionist, some industries relied on what he calls “regulatory unionism”. These industries relied on sectoral collective bargaining and the enforcement of standard wage rates by industry unions in order to regulate wage competition within the industry. He argues that in the 1920s US “[e]mployers often accepted industrial unions in exchange for the cost those unions could force on competitors and just as often resisted them in order to maintain the advantage of open-shop wages” (Gordon 1994: 127). Similarly, he argues that the Wagner Act of 1935, which established nationwide labor rights, was tacitly accepted by some business groups and claims that without that “there is little likelihood that it would have passed” (Gordon 1994: 205). Gordon argues that

the progressive turn of the “second New Deal” was part and parcel of two decades of business strategy and two years of business-driven recovery politics. In historical memory, of course, the New Deal is virtually synonymous with a transformation of labor relations and labor law. Yet the emergence of industrial unionism and a “common law” of labor relations was not (as it is commonly portrayed) simply the product of an emboldened labor movement, an enlightened state, or a momentarily weakened business community. (Gordon 1994: 2)

Similarly to Swenson, Gordon claims that important business groups favored the New Deal reforms and played an important role in shaping its legislation. Different from Swenson, though, Gordon does not argue that business support for social policies resulted from

invariable economic interests of specific types of firms. Instead, he highlights specific historical experiences made by US business during the 1920s and the inconsistencies and deficiencies of state social policies to explain business support for federal social policies. He also notes that soon after the passing of the Social Security Act in 1935 business groups originally supportive of SSA turned into vocal opponents as they realized that the Act failed to standardize labor costs across states. The argument made by Gordon does thus not imply that specific types of firms would be generally supportive of social policies and does, instead, emphasize effects of political institutions on competitive dynamics in federalist systems.

The interpretation of business involvement in the New Deal offered by Gordon and by Swenson is in sharp contrast to the one presented in a study by Hacker and Pierson (Hacker and Pierson 2002). These authors explain the passing of the Social Security Act as a result of a temporary political weakness of business, caused by the Great Depression and the shift of social policy-making from the state to the federal level during the Roosevelt administration. Building on the assumption that the structural power of business derives from its capacity to relocate production, Hacker and Pierson argue that “[w]ith the shift of political action to Washington, the structural power of business declined dramatically.” (Hacker and Pierson 2002:305).

According to Hacker and Pierson, business benefited politically from the federated nature of the US polity. During the 1920s, the scope and content of social policy initiatives at state level had been limited primarily because of fear of business opposition and the relocation of capital to other states: “fear of business disapproval was the principle obstacle to reform” (Hacker and Pierson 2002: 290). This situation of competitive federalism was exploited by employers to constrain reform initiatives: “Employers did act, with considerable success, to water down bills wherever possible. Similarly, they fought successfully to block national legislation, out of fear that it would open the door to federal intervention on other social policy issues.” (Hacker and Pierson 2002: 292). The outcome of this situation was that very few and limited reforms were passed in the pre-New Deal era that significantly raised labor costs for firms engaged in inter-state competition (293).

The shift of policy-making from state capitals to Washington during the New Deal-era fundamentally altered the balance of power and made the passing of federal welfare laws possible, argue Hacker and Pierson. Some business groups accommodated to this change in the balance of power and decided to support federal social legislation for strategic reasons:

impetus for the SSA came largely from outside the business community and ... most employers strongly opposed the enactment of a national system of social insurance.Even within the small faction of employers who supported the SSA, whether quietly or vocally, many did so only because they feared that the alternative would be worse. In other words, support for the SSA often represented a strategic response to a loss of political power. Once one attends to the significance of anticipated reactions, it becomes clearer that only a sharp decline in business power made the SSA possible (Hacker and Pierson 2002: 298).

The interpretations by Gordon and by Hacker and Pierson do thus contrast sharply with respect to the assumed relationship between business interests and federalist institutions. While the analysis by Gordon suggests that important business groups tried to overcome federated social policy legislation by lobbying for nationally uniform regulation, the analysis by Hacker and Pierson stresses that the shift from state to federal regulation resulted not from the active efforts of business groups, but, to the contrary, from a temporary political weakening of business. The contrasting claims made by these and other scholars suggest that further research on the role of business interests in social policy development is necessary.

While the studies by Gordon and by Hacker and Pierson focus on the role of federalist political institutions in shaping employer attitudes and strategies with respect to welfare state development, other studies have focused on *economic* interests of firms, i.e. interests generated by the industrial production process itself, rather than by the political environment. Of particular importance in this respect is the extensive work on employers by Isabela Mares. Mares analyzes the role of employers in the historical construction of welfare state programmes in France and Germany, focusing on work injury insurance, unemployment insurance and early retirement (Mares 2003a, 2003b, 1997). Her main goal is “to understand how the welfare state...generates benefits, opportunities or institutional advantages to firms” (Mares 1999: 17). She finds that “[t]he empirical evidence disconfirming the proposition that the welfare state has been enacted against the opposition of employers is simply overwhelming”. To the contrary, she argues, “most social policy outcomes were supported by broad *cross-class alliances* that comprised both trade unions and representatives of the business community” (Mares 2003a: 260, emphasis in original).

Mares presents a theoretical model that builds on conflicts between different types of firms on the economic utility of different types of social policies. According to her model, inter-sectoral conflicts within the business community will, under certain conditions, lead to the deliberate formation of cross-class alliances in favor of public social policies. Such cross-class alliances constitute a deliberate and strategically motivated collaboration between segments of the business community and representatives of the labor movement. The

theoretical model specifies two particular reasons why important segments of the business community may support social policies. One is the interest of certain types of firms in protecting skill investments, and the other the interests of certain types of firms in redistributing social risks across sectors:

The preoccupation of firms with social policies has been shaped by two underlying considerations. On the one hand, employers have attempted to institutionalize guarantees that the investment in the skills of their employees can be maintained during interruptions of the employment relationship: sickness, disability, unemployment. On the other hand, firms have attempted to share (or offset) the costs associated with the incidence of these risks, by supporting the formation of highly redistributive risk pools. The cause of inter-sectoral disagreement among employers has its origin in the different priorities attached by firms to these two objectives - guarantees to their investment in skills and risk redistribution (Mares 1999: 58).

According to Mares, these two motivations, skill investments and risk redistribution, explain why dominant groups of employers supported the formation of social policies in the two countries studied, France and Germany. For instance, the interest in skill investments motivated firms relying on skilled labor to favor a contribution-based system of unemployment insurance, while firms not relying on skilled labor opposed unemployment insurance, according to Mares (Mares 1999: 398-9). Similarly, sectors with a high risk of work accidents pushed for a public scheme of work accident insurance, in order to share the costs of compensating injured workers with other, low-risk, sectors, thereby redistributing the risk across the economy. Therefore, Mares argues, that “under some conditions, social policies provide distinct institutional advantages to firms” (Mares 2003a: 23). The finding that specific types of employers had supported specific social policies leads Mares to question the importance of class conflicts as a driving force of social policy development:

These propositions, showing that even profit-maximizing firms have (under specific circumstances) an interest in the provision of social insurance, allow us to *reject a class-based perspective* on the development of the modern welfare state, according to which labor favors and employers oppose the introduction of social insurance (Mares 2003a: 62, emphasis added by TP).

Like Swenson, also Mares tends to de-emphasize the importance of political constraints in shaping employers' positions and strategies. Mares acknowledges that employers did not act as agenda setters in welfare state development (Mares 2003a: 259) and that their support for certain social policies often reflected a strategic response to political constraints (Mares 1999: 58; 2003a: 50-62). However, these acknowledgements are at odds with the gist of her theoretical model, which builds on the *pre-strategic* (genuine) preferences of employers, rather than on strategic preferences. The tension between an explanation based

on pre-strategic preferences, and an explanation based on strategic preferences remains under-explored. In short, the limitations of this strand of research warrant further research to find out whether employers' acceptance of specific social policies was based on pre-strategic or strategic preferences.

Moreover, the approach taken by Mares runs the risk of taking the positions and demands issued by various employer organizations during the reform process as valid expressions of their non-strategic preferences, rather than as a complex outcome shaped by non-strategic preferences and strategic adjustments to the political context alike. The underlying assumption seems to be that the political behavior of employer organizations is an unproblematic indicator of the economic interests of the firms they represent. This approach, however, lacks a systematic analysis of the broader political context. Differences in the broader political context, such as the balance of power among the political actors, policy legacies or the kind of polity employers operated in, are not systematically analyzed or controlled for³.

Employer-centred explanations and the VoC approach

Employer interests in skill investments play an important role also in the Varieties of Capitalism approach, which the cross-class coalition thesis is partly informed by. The primary intention of the VoC approach appears to be to explain the continued cross-national divergence in political-economic institutions, rather than the historical origins of distinct national models. Nevertheless some scholars, like Isabela Mares, draw on elements of the VoC approach, to support their arguments about employer preferences.⁴

The VoC approach highlights the importance of social policies for skill formation (Hall and Soskice 2001: 50-51). Social protection may serve as a solution to market failures in skill formation (Iversen 2005: 9). The VoC approach distinguishes between *general* skills,

³ Mares claims to control for differences in political variables: "The six cases analyzed in this dissertation allow for a broad variation across a broad number of crucial independent variables – such as the sectoral balance of power among employers, the influence of employers in the policy-making process, labor strength, relative autonomy of bureaucratic elites, etc." (Mares 1999: 63-4). In fact, it is however not evident how her analysis does so. There is a remarkable absence of any systematic discussion of these variables in the empirical analysis.

⁴ To clarify, I do not intend to imply that an employer-centred explanation of welfare state development would be essential for the VoC approach. While employer-centred explanations do, in part, rely on the VoC approach, the core tenets of the VoC approach do not necessarily require an employer-centred explanation. Core components of the VoC framework, including institutional complementarities, may also have emerged through mechanisms other than purposive political actions by employers. They may also have emerged the unintended consequences or by-products of past distributive conflicts. This latter interpretation, I believe, is compatible with the core tenets of the VoC framework. I thank my co-supervisor, Prof. Martin Rhodes, for pointing out this distinction to me.

which are transferable across firms and sectors, and *asset-specific* skills, which are tied to specific firms or sectors (Estévez-Abe et al. 2001: 148; Iversen 2005: 10-11). According to the VoC approach, investing in asset-specific skills exposes workers to higher risks of unemployment and potential income loss, as these skills cannot be transferred to other firms or sectors. Social policies serve to protect investments in specific skills by protecting workers with such skills from income losses due to unemployment. In the absence of social policies protecting specific skills, workers will face strong incentives to invest in general skills, rather than asset-specific skills, resulting in an underinvestment in specific skills. Employment protection, unemployment insurance and collective wage bargaining are seen therefore as policies relevant for the protection of specific skills (Estévez-Abe et al. 2001: 150).

Torben Iversen builds on this insight to construct a theory of welfare state development that tries to explain cross-national differences with the help of different skill profiles existing in these countries (Iversen 2005). According to the explanation he presents, demand for social insurance stems from the asset specificity of skills. To simplify, Iversen argues that in economies that rely on asset-specific skills demand for social protection from workers, and also employers, will be strong. In economies that rely on general skills, instead, there will be very little demand for social protection, neither from employers, nor from workers, because workers can easily switch to different jobs and therefore do not depend on social protection. Iversen suggests that “employers who are pursuing product market strategies that require specific skills also have a vested interest in social policies that reduce the risk of acquiring those skills” (Iversen 2005: 12). This assumed interest leads him and his collaborators to the hypothesis that “social protection often stems from the strength rather than the weakness of employers” (Estévez-Abe et al. 2001: 181) .

Extending this argument, Iversen, Cusack and Soskice (2007) argue that differences in national skill profiles may even explain why different countries have adopted different electoral institutions. Noting that most coordinated market economies have proportional representation (PR) systems, while most liberal market economies have majoritarian electoral systems, they propose that the adoption of different electoral systems may have been a result of differences in economic organization and skill profiles. In countries that relied on asset-specific skills, employers and workers both had an interest in institutions that facilitated and regulated cooperation and coordination, whereby the PR system is one such institution. These scholars thus put forward the proposition that “PR was adopted to ensure a political system that protected investments in co-specific assets in locally coordinated economies around 1900,

while majoritarian systems undermined such protection” (Cusack et al. 2007: 388). In short, as the title of their article suggests, economic interests explain the origins of electoral systems.

To sum up, skill formation thesis builds on the assumption that issues of skill formation are of decisive importance for the way employers view social policies and political institutions. Iversen is cautious not to present the welfare state as the straightforward outcome of employer demands and, instead, builds his model primarily on the effects of national skill profiles on electoral politics (2005: 12-14). However, other scholars, like Mares, do rely on the proactive role of employers to link skill profiles to welfare state construction (Mares 2003b: 39). She argues that employers have an interest in social policies, because “social policies play an important role for the labor market strategies of firms: they reduce the reluctance of workers to invest in skills” (Mares 2003a: 9). The skill formation thesis attributes pivotal importance to the issue of skill investments in order to understand the way business perceives the welfare state. Firms’ need for productive efficiency is seen as the principal component of an explanation of welfare state development based on purposive action.

While arguments derived from the VoC approach do, in part, inspire economic-functionalist explanations of employers’ role in welfare state development, as shown in this section, the overlap between employer-centred explanations and the VoC approach is only a partial one. Some proponents of the VoC approach do not endorse employer-centred explanations. In a defense of the VoC perspective on institutional change, Hall and Thelen, for instance, point out that they “think it dangerous to assume that the institutions of the political economy were originally created to serve the interests they advance at much later periods of time” (Hall and Thelen 2009: 14). In a similar vein, Hancké et al point out that “capital may indeed be crucial in capitalist economies, but, paraphrasing Marx, it does not choose the conditions under which it operates” (Hancké et al. 2007: 19). Rather than endorsing employer-centred explanations of welfare state development, these proponents of the VoC approach put forward a model of employer behavior that emphasizes changes in employer preferences in response to institutional adjustment, as we will see in more detail below.

Vice versa, not all proponents of employer-centred explanations are inspired by the VoC approach, as the work by Colin Gordon, discussed above, shows (Gordon 1991, 1994). Gordon emphasizes specific historical experiences made by US firms, as well as unwelcome disparities in competitive conditions created by the federated nature of the US polity, rather

than hard-wired economic interests, to explain support by American industrialists for the New Deal legislation. The work by Gordon thus provides a non-functionalist version of an employer-centred explanation.

Organizational approaches to employer politics

A different approach to employers' role in social policy-making is applied by scholars focusing on the organizational characteristics of employer associations, rather than on characteristics of individual firms. This approach builds on research about corporatist forms of interest representation and the role of economic interest groups in public policy making and policy administration (Crouch 1994; Traxler 1986; Schmitter and Streeck 1981; Streeck and Schmitter 1985). Inspired by this work on the role of corporatist institutions, some scholars have analyzed the impact of the organizational characteristics of employer associations on their social policy positions. Of particular importance in this respect is the work by Cathie Jo Martin and Duane Swank (Martin 1995, 2000; Swank and Martin 2001; Martin and Swank 2004; Martin 2004, 2006).

Martin and Swank have analyzed, for instance, the correlation between spending on active labor market policy and the way employers are organized in various countries. They find that "the centralization of representational power, coordination across [associational] units, and integration of associations in corporatist policy-making forums result in greater employer support for and participation in social policy formation and implementation" (Martin and Swank 2004: 594). Moreover, in a different study, they conclude that "the organization of employers is one of the most important determinants of cross-national and temporal variations in total social welfare effort. Where employers are centralized, cohesive, and economically coordinated, social welfare effort is greater." (Swank and Martin 2001: 890).

Like Mares and Swenson, Martin and Swank also emphasize that employer organizations had a positive, rather than a constraining or retarding effect on welfare state development. Martin and Swank do, however, take a different theoretical approach. They do not root employers' support or participation in social policy formulation in fixed economic interests, but, instead, in characteristics of the institutional environment and organizational features of these associations. Their work constitutes a valuable theoretical advancement in embedding employer politics in political context. Nevertheless, the validity of their findings is limited by their strong reliance on statistical correlations. Although Martin and Swank rely on

a sophisticated combination of qualitative and quantitative methods, their argument rests strongly on their findings of significant statistical correlations between organizational-institutional variables and social expenditures.

The causal mechanisms creating the correlation between the two sets of variables require more detailed empirical investigation to check whether these correlations are non-spurious and correctly specified. Employer organization and social spending may, for instance, be the joint outcome of a third variable or background condition. Historical process-tracing analysis is necessary, I argue, to identify the real impact of employer organizations on welfare state development as well as the motivations for employer organizations to support specific policies.

Critics of the cross-class coalition thesis

Several studies have criticized the cross-class coalition thesis for neglecting the importance of structural constraints compelling employers to accept welfare state programmes and institutions. Through historical case studies of several countries, Huber and Stephens have found that employers consented to labor market and social policies only in the context of hegemonic labor movements (Huber and Stephens 2001). Their study finds that business acceptance of social democratic social policies “was limited to the period in which the social democratic parties and the associated labor movements were near hegemonic and their social policy initiatives in particular enjoyed broad popular support” (Huber and Stephens 2001: 9). Huber and Stephens point out that “the constraints of the larger power distribution and the institutional context shape the preferences and strategies of these actors to begin with” (Huber and Stephens 2001: 33).

Similarly, Hacker and Pierson, in their study discussed above, argue that shifts in the political balance of power motivated US business groups to accommodate to existing constraints and collaborate with government policy-makers in drafting social legislation. Hacker and Pierson find that the influence of business on social policy making varied greatly across time and institutional contexts, whereby changes in institutions also changed “the scope and character of business power” (Hacker and Pierson 2002: 315). Hacker and Pierson criticize existing research supporting the cross-class coalition thesis for failing to deal with three types of theoretical and methodological challenges: a failure to distinguish between multiple mechanisms of business influence, misspecification of the genuine preferences of

business groups, and the inference of business influence from an *ex post* correlation between the stated business preferences and political outcomes (Hacker and Pierson 2002: 278).

In an analysis of the Swedish case, Korpi finds that employers had not been protagonists of welfare state development in this country. Instead, social democratic dominance had shifted the feasible range of policy options for employers in such a way that they decided to consent to some policies (Korpi 2006: 186-193). The alternative view of business as antagonistic to social policies, which emerges from his historical analysis, leads Korpi to reject the employer-centred explanation of the welfare state as empirically unfounded:

Employer-centered scholars ... have apparently misinterpreted employer consent to reform proposals from the left as evidence of their first-order preferences for welfare state expansion. Crucially, employer-centered research has not yet presented empirical evidence indicating that employers have been protagonists with first-order preferences for major reforms extending social citizenship rights (Korpi 2006: 202).

The analytical approach adopted in this thesis builds on the arguments made in these studies. These studies are all informed by what I call the “*political accommodation*” approach. This approach emphasizes the way political constraints shape business positions and influence in welfare state development. Rather than taking stated business preferences as an independent causal factor driving welfare state development, these studies endogenize stated preferences in the political context. Thereby they are able to challenge the economic efficiency-based explanations provided by the cross-class coalition thesis. They argue that employers had accepted social policies not because they expected to gain economic efficiency benefits, but because they decided to adapt to changing political contexts. Moreover, while the cross-class coalition approach tends to see employers as active supporters of welfare state development, these studies see employers as mere passive consenters. In short, the cross-class coalition approach and the political accommodation approach provide very different explanations and understandings of the role of employers in welfare state development, and thereby also of its driving forces.

1.II Case Selection: Germany as a Crucial Case

The thesis relies on a *historical within-case analysis* of the German case. Germany constitutes a *crucial case* for the testing of the two alternative arguments of this thesis. A case is crucial if “it is most, or least, likely to fulfill a theoretical prediction” as John Gerring reminds us

(2007: 115). Germany is a crucial case in this sense because its institutional setting benefits the production strategies of predominant types of firms in various ways. Studies in comparative political economy, dealing with cross-national diversities in production regimes, have identified Germany as a paradigmatic case of a type of market economy that is characterized by an institutional configuration that generates higher productivity and competitive advantages for firms⁵ (e.g. Thelen 2001; Hassel 2007; Dore 2000; Hall 2007; Streeck 1992; Hall and Soskice 2001).

For this reason it appears plausible that German employers may also be more supportive of institutions of social compromise and social protection than their counterparts in other countries. Moreover, because of the economic advantages to firms provided by its institutional setting, Germany arguably provides a most likely case for explanations that attribute employers a crucial role in the historical formation of this model. If economic-functionalist models of employer preferences in social policies are valid, the evidence in their favor should be the strongest in the German case. Germany is thus a case, I argue, where also the cross-class coalition thesis should be most likely to hold. If, in contrast, the cross-class coalition thesis does not hold in this country, it is even less likely to hold in countries where the efficiency effects and competitive advantages of the institutional setting are less pronounced.

The variegated ways in which firms in advanced welfare states make use of existing policies and institutions have been studied widely, such as, for instance, the usage of early retirement schemes for workforce restructuring (Ebbinghaus 2001, 2006; Trampusch 2005) and advantages with respect to skill formation (Estévez-Abe et al. 2001). Other scholars have focused on how industrial relations institutions are used by firms to benefit their production strategies. Wolfgang Streeck, in particular, argued that Germany's industrial relations institutions have facilitated the pursuit of a strategy of so-called "diversified quality production" by German firms (Streeck 1992: 4-10). Streeck conceptualizes institutions as constraints as well as resources for firms. They operate by "imposing enforceable social constraints on rational market participants, as well as offering them effective opportunities to restructure towards higher product diversity and quality" (Streeck 1992: 4). Co-determination is one important institution analyzed by Streeck. He argues that co-determination "has significantly changed the way in which employers utilize labor as a factor of production"

⁵ To clarify, this thesis is not concerned with the question of whether labor market and social policies actually create economic efficiency benefits, but with the question of whether expectations of such economic efficiency benefits have motivated employers to support these policies.

(1992: 137) and, because of this, “has not merely posed a problem for enterprises but has also offered a solution” (1992: 160).

While these studies are interested primarily in the consequences of institutions and their usage by individual firms, rather than in their political origins, they clearly have implications also for the study of employers’ role in policy-making. In principle, one can think of two alternative types of explanations for the emergence of institutions and policies that turned out as beneficial for specific types of firms. One possibility is that institutions that have turned out to be beneficial for firms may have been initially imposed upon firms that were unaware about their future economic advantages. This perspective is implied in some of the work by Streeck. He emphasizes in particular the importance of ongoing processes of piecemeal improvisation and experimentation within institutional constraints, over time possibly leading to “institutional fit” (Streeck 2001: 31). Alternatively, one may argue that far-sighted employers have played a constitutive role in the construction of these institutions, trying to deliberately engineer institutional solutions to problems created by the production process. This perspective is suggested, for instance, by some scholars relying on the VoC approach⁶ (e.g. Hall and Soskice 2001: 50-1; Cusack et al. 2007).

As mentioned, Germany constitutes a *most likely case* for the second hypothesis, given that the existence of competitive advantages and institutional efficiency effects has been most extensively researched and documented for this country. If expectations of economic efficiency benefits have been an important reason for employers to support the construction of labor market and social policies, we can expect that Germany is where this is most likely to be the case. If, to the contrary, we find that expectations of economic efficiency benefits played only a marginal or no role at all for employers, this would also reduce the probability that such benefits are able to explain employer behavior in other countries, where economic efficiency benefits will presumably be likely to be less pronounced. Therefore, I claim, Germany attains the status of a crucial case.

The choice of “policy cases”

The thesis focuses on the role of industrial employers in the construction of those policies and institutions that, in retrospect, came to characterize the German model of political economy. Thereby, the thesis focuses on those “unsettled moments” of history during which these

⁶ As mentioned above, this second perspective is not shared by all scholars using the VoC framework (Hall and Thelen 2009: 14) (Hancké et al. 2007: 19).

policies have been constructed, rather than on the day-to-day policy making during more settled times, because we can assume that it is during these moments of policy construction that the preferences of political actors are likely to matter most.

The empirical analysis focuses on a set of “policy cases” that are central to the German model of political economy, in particular, the policies of the Bismarckian welfare state, sectoral wage bargaining and co-determination. The rationale behind the selection of these “policy cases” has been to choose policies that provide plausible and relevant test cases for both of the two alternative theoretical perspectives that are at the center of the thesis, the economic-functionalist perspective of the cross-class coalition thesis and the political-strategic perspective of the political accommodation thesis. This means that I have chosen such policies that arguably are labor-friendly and at the same time are associated with economic benefits for firms, therefore being of relevance for the testing of the relative role of economic interests and strategic accommodation.⁷

I chose to focus on the formation of the Bismarckian social programmes of the German welfare state (chapters 3, 5 and 7), because this type of social policies is at the center of arguments about the importance of social policy to firms. The employment-based social insurance schemes of the Bismarckian welfare state support corporate strategies of German firms in various ways, in particular by reassuring workers that their skill investments are protected against economic volatilities, as argued, for instance, by Estevez-Abe et al (2001; s.a. Hall and Soskice 2001: 50-1). Understandably, proponents of employer-centred explanations of welfare state development have thus often focused their analysis on social insurance programmes, in particular, the extensive work by Isabela Mares (Mares 2003a, 2003b, 2001, 1999, 1997). Means-tested or universal types of social policy⁸, like social assistance or social housing, are not analyzed in the thesis, not only because they are comparatively under-developed in the German case, but, more importantly, because they would not provide a relevant test case for the economic-functionalist argument.

In addition to social insurance policies, I chose to focus on the domain of *industrial relations*, as another institutional domain that supports specific corporate strategies. In chapter 2, the thesis looks at the motivations of firms to form employer associations and to start with

⁷ To clarify, the selection of “policy cases” is based on their general relevance for the two theoretical perspectives, rather than on whether individual proponents of either of the two approaches have actually made empirical claims about these specific cases.

⁸ Welfare state research distinguishes between different types of social policy. Other types of social policy programmes are, in particular, means-tested programmes and universal, flat-rate benefit programmes. See, in particular, Esping-Andersen (1990) and Titmuss (1958).

collective bargaining in the late 19th century. I chose this case because today employer associations and sectoral bargaining provide firms with important resources for coordination and for cooperation with organized labor. Sectoral bargaining not only secures industrial peace, it also prevents firms relying on skilled labor from labor poaching by other firms, as pointed out by Hall and Soskice (Hall and Soskice 2001: 24-5). Following an economic-functionalist perspective we should thus expect that employers may also have played a role in the historical formation of sectoral bargaining institutions.

The Stinnes-Legien agreement (chapter 4) is included because this agreement between capital and labor institutionalized sectoral bargaining and works councils, and, thus, became the founding charter of the German model of industrial relations. As shown, for instance, by Kathleen Thelen, in the Federal Republic German firms managed to use works councils as an instrument for securing cooperative labor relations at the workplace (Thelen 1991). Therefore, also the Stinnes-Legien agreement provides a plausible test case for the two alternative theoretical perspectives. For a similar reason, the thesis includes also the case of co-determination in the supervisory boards (chapter 8), a core element of the German model, and often seen as facilitating cooperative labor relations and employee loyalty to the firm.

The choice of organizations

The empirical focus of the thesis is on the peak-level federations representing German employers⁹, rather than on their sector-level associations. These federations are the CDI (*Central Association of German Industry*) during the German Empire, the VDA (*Federation of German Employer Associations*) in the Weimar Republic, and the BDA (*Confederation of German Employer Associations*) in the Federal Republic. These three organizations acted as the principal political representatives of industrial employers in the development of the welfare state and industrial relations in Germany. The reason for the choice of peak-level organizations, rather than sectoral ones, is that in Germany the social policy interests of employers are represented in the political sphere predominantly by their peak-level federation, rather than by their sectoral associations.

The emphasis by the cross-class coalition thesis on cross-sectoral conflicts would suggest a focus on sectoral employer associations, rather than on the peak-level federations.

⁹ Business interests are represented in the German polity by three types of organizations: a) employer organizations, which represent the labor market interests of firms; b) sectoral trade and industry associations, which represent the product market interests of their members; and c) the chamber of commerce, which deal, inter alia, with organizing vocational training and the licensing of firms

However, due to the way sectoral interests are aggregated within the German system of interest representation, hypotheses building on sectoral cleavages are empirically difficult to test. A division of labor between peak-level and sectoral associations mandates sectoral associations with the task of collective bargaining with unions, and the peak-level federation with the task of representing employer interests vis-à-vis the government, other political actors and the public in general (see e.g. Grote et al. 2007: table 8.5). Sectoral interests and preferences are aggregated internally by the employer associations and are then represented in the policy-making process by the peak-level. Sectoral associations do not normally issue policy statements on those issues covered by the peak-level or do so only in order to second the peak-level. This means that potential sectoral differences cannot normally be observed in the policy-making process, although such differences may still exist and lead to tensions within the employer camp, occasionally even preventing the peak-level to take a clear stance. The intransparency of employer associations' internal decision-making does, however, make it difficult to analyze such potential intra-business differences in a systematic way.

The empirical analysis in this thesis suggests that in welfare state development sectoral conflicts tended to be subordinate to class conflicts. As mentioned above, this is in part the result of the way sectoral interests are aggregated by the peak-level federation. More importantly, though, the existence of a common opponent, a reformist government or an assertive labor movement, often united employers and allowed the peak-level federation to contain potential internal differences in favor of the articulation of a common stance in policy-making, though the capacity of the peak-level federation to do so declined considerably recently (for the reasons of this see chapter 9). Where they are observable, sectoral differences tend to concern specific policy details, rather than positions towards a social policy as such. To mention a characteristic example, the introduction of work injury insurance in the early 1880s was generally supported by industrialists as an important means of pacifying a discontent working class. Still, sectoral differences existed concerning the question of how the costs should be spread across sectors (see chapter 3.II). Moreover, where intra-business differences are found to matter, their reasons are diverse and difficult to generalize.

1.III The Argument in Brief

The argument put forward in this thesis provides an alternative to economic-functionalist explanations of employers' role in welfare state development by building on insights from historical institutionalism and the power resource approach. The thesis shows, first, that

employers were often quite reluctant to accept the introduction of new social policies or the expansion of existing ones. Second, the thesis shows that when employers accepted social reforms they typically did so not because they expected benefits in terms of economic efficiency or competitiveness but for strategic reasons, in order to prevent even less favorable outcomes. The thesis thus presents an explanation of employers' role in welfare state development that is complementary to labor-centered explanations, rather than in opposition to the latter.

The main argument advanced in this thesis is that political constraints compelled industrial employers to accept certain social policies as options reflecting lesser evils. While the *economic* interest of employers was to prevent the formation of social policies, *political-strategic* considerations sometimes turned employers into supporters of certain social policies. Their embeddedness in a specific historical political context shaped what employers thought is the best they could achieve in a given situation. Policy positions thus need to be linked to political context. They need to be seen as endogenous to politics, rather than be taken as given or exogenous to our theories. The embeddedness in the political context produces strategically motivated behavior and political accommodation. As Hacker and Pierson have aptly pointed out:

a group's actions often will not reveal its preferences but rather its strategic calculations of what is the best that can be accomplished given existing circumstances. An actor's expressed policy preferences may in fact be "induced" or "strategic" - that is, they reflect accommodations to circumstances that constrain what can be achieved (Hacker and Pierson 2002: 283).

To analyze the importance of the political context, I identify three broad historical periods, which are characterized by different patterns of political behavior by employers towards welfare state policies and institutions of social compromise. The first period is the period of the Wilhelmine German Empire (1871-1918) During this period industrial employers in Germany pursued strategy of *social pacification*. This period was characterized by a rapid growth of the labor movement, which was opposed by a close alliance made up of industry, agriculture and government. Employers' political behavior during this period was shaped by the goal of regaining the consent of the working class to the existing political-economic regime and to suppress the socialist labor movement. Employers supported the Bismarckian social reforms during the 1880s and made far-reaching concessions to labor union leaders in the Stinnes-Legien agreement in 1918 with the goal of crushing the socialist labor movement or radical elements within it, respectively.

During the second period, the Weimar Republic, German employers pursued a strategy of contention, attacking existing unwelcome policies and institutions, while at the same time cooperating in the construction of new policies to replace older ones, where political majorities made outright dismantling of unwelcome social policies an unviable strategy. In particular, employers focused their attacks on the eight hour working day, which they had already previously accepted, and forms of state intervention in industrial relations. They tried to get rid of the unemployment assistance programme by replacing it with a more restrictive programme of unemployment insurance, which allowed more control over benefit recipients. The resurgence of class warfare, which gained momentum with the start of the world economic crisis in 1929, contributed to the collapse of the Weimar Republic. Industrial employers had lost trust in the problem-solving capacities of democratic institutions and pinned their hopes on authoritarian solutions.

In the third period, the Federal Republic (since 1949), the political behavior of employers became shaped by a *politics of containment*. This period was characterized by rising economic prosperity (the “economic miracle”) and an expansion of welfare state policies driven by electoral competition. In this context, employers tried to limit the scope and generosity of existing social policy programmes, while at the same time accepting the need for social compromise. At the same time, they tried to prevent more thorough-going reforms in the organization of the economy, which were demanded by the labor unions and threatened to curtail entrepreneurial control over investments and decisively shift power in the economy to organized labor. More recently, during the 1990s, employers shifted away from social compromise and political accommodation, prioritizing welfare state retrenchment and lower tax burdens. The secular rise in payroll taxes, interacting with the internationalization of the economy, had eroded employers’ willingness to compromise.

Linking political behavior to periodisation, as I do here, allows us to understand how large-scale historical changes have changed the goals and strategies of employer organizations. Clearly, this periodisation of goals and strategies involves some simplification. In each period we can find a combination of motivations shaping employers’ political behavior, rather than just a single one. Cost containment has always been a concern of employers throughout history, and not only in the post-war period. To give an example, employers supported the introduction of social insurance in the 1880s in order to pacify the working class, but their participation in the policy-making process was, at the same time, also motivated by a concern to avoid an undue increase in labor costs as a result of the new

programmes. Cost containment had not been employers' main concern during this period, however, because protective tariffs shielded the dominant sectors from international competition. Similarly, social pacification continues to play a role also in the post-war Federal Republic, evident, for instance, in the use of early retirement for the purpose of peaceful labor shedding. Yet, the importance of this goal for defining employers' policy positions has greatly declined compared to the German Empire. While each period involves a combination of different goals, we can nevertheless identify a dominant pattern in each period.

The types of challenges that employers responded to in their policy positions changed over time. The thesis highlights two types of challenges: (i) threats of social and an associated collectivization of industry; and (ii) unfavorable policy proposals on the political agenda. Employers responded to the first with a politics of *labor pacification*, and to the latter with a politics of *containment*. First, employers' support for social policies was motivated by the goal of pacifying the working class in the context of widespread political discontent among workers, which made them susceptible to revolutionary agitation. This goal crystallized in the context of a rising and militant labor movement, seen by employers as a revolutionary menace, determined to expropriate the industrialists. In this context, industrialists aligned with the authoritarian government of Bismarck to introduce social programmes that were intended to tie the interests of the working class to the existing political-economic order and cut off their support to the opposition Social Democrats and the labor unions. Similarly, after the collapse of the Wilhelmine Empire in 1918, the goal of warding off a Soviet-style social revolution motivated industrialists to make far-reaching concessions to moderate union leaders. Social protection and institutions for social compromise served as means to prevent a socialist revolution.

The second reason for employers to consent to labor market and social policies was strategic in nature. To avoid becoming irrelevant bystanders to ambitious reform initiatives that appeared likely to succeed, they decided to cooperate, often with the motive of taking the edge off the planned policy. Often such behavior involved the strategic endorsement of more moderate policy proposals. Exercising effective influence on reform outcomes requires accommodating to the goals of reformers. When reform projects apparently cannot be stopped entirely, trying to gain some influence over the design of important details of the proposed legislation is a more promising strategy for influencing the outcome, compared to fundamental opposition. Therefore, employers often directed their opposition not against a planned policy as such, but against specific details, for instance, the mode of financing or the

mode of benefit calculation, in order to prevent an undue rise in social expenditures. Employers often decided to cooperate in the drafting of social legislation as a way of influencing the proposed policy, because this appeared as a more promising strategy of influence compared to fundamental opposition, even if, at heart, they remained indifferent to the goals of the proposed policy.

Strategic accommodation is a response to political constraints. Two types of constraints are of particular importance: policy legacies and the balance of power among the relevant political actors. They reflect the past and the present balance of power among the actors, respectively. First, *policy legacies* are a powerful constraint on what actors can expect to be able to achieve. Policy legacies are the result of policies adopted in the past. They constitute the policy *status quo* against which political actors need to evaluate the value of any alternative policy options. Political actors do not evaluate concrete policy options against the background of a “clean slate,” but against the background of the existing policy status quo. Is the alternative policy option likely to constitute an improvement or a deterioration compared to the status quo? The formulation of policy preferences and positions is thus likely to be strongly influenced by policy legacies. Decisions made in the past also constrain the range of options that are on the agenda in the present, by precluding certain options.

Second, the balance of power among political actors in the present limits the range of policy options that are politically viable. Political majorities in favor or against their own policy preferences define the extent to which political actors are likely to accommodate to the political context. Political majorities against an actor’s own first-order preferences will induce an actor to deviate from this ideal point and adjust its positions to bring them more in line with the politically viable policy options. In such a situation, an actor’s expressed stance reflects its second-best option and is intended to prevent the adoption of a policy option that, from the view of this actor, would be even worse.

Employers have often decided to support specific social policy choices in order to either prevent or dismantle other policies that they considered to be even less beneficial. Disliked policy legacies have motivated employers to support policy alternatives that helped them to do away with the disliked policy, in contexts where demanding the entire dismantling of the existing policy without replacement would have been politically not viable. In addition, the prospect of influencing important details of proposed legislation compelled them to cooperate. Exercising influence on government policy-making is linked to a willingness to cooperate and to go along with the broad political objectives of social reformers. German

employer organizations have been and continue to be well aware of this. Moreover, their decisions to participate in the design of new social policies is also intended to maintain good relations with government, in addition to influencing the design of the specific policy at hand, as good relations facilitate influence.

The theoretical argument presented in this thesis builds on *microfoundations* different from the ones of the cross-class coalition thesis. According to the cross-class coalition thesis, business support for social policy formation was the result not only of strategic considerations, but, more importantly, of genuine interests of important segments of business (see e.g. Mares 1999: 58-60; Swenson 2002: 11). As elaborated in section I above, the cross-class coalition thesis supplies microfoundations to its argument by building on the importance of skill investments. In contrast, the microfoundations of the argument advanced in this thesis build on the decommodification thesis developed by Esping-Andersen (Esping-Andersen 1990: 22). According to this thesis, social policies reduce workers' dependence on market income by providing alternative sources of income, a policy effect that is called decommodification. Decommodification reduces the dependence of workers on gainful employment and, thus, also on their employer. In Esping-Andersen's typology, welfare state regimes differ in the extent to which they decommodify workers, whereby "the Scandinavian welfare states tend to be the most de-commodifying, the Anglo-Saxon the least" (Esping-Andersen 1990: 23), with the Continental welfare states lying in between.

Employers can be expected to oppose decommodification because it reduces work incentives and is likely to diminish work effort and work discipline. Decommodification reduces work incentives by raising workers' reservation wage. As argued by Esping-Andersen, decommodification "strengthens the worker and weakens the absolute authority of the employer. It is for exactly this reason that employers have always opposed decommodification" (1990: 22). As subsequent chapters will show (3,5 and 7), employers' interest in limiting decommodification translated into a preference for tying benefit entitlements closely to employment, given a context where the complete absence of social policy was politically not feasible. Opposition to decommodification made employers prefer Bismarckian social insurance policies to universal social policies, as the latter are more decommodifying. A genuine economic interest in limiting decommodification combined with political-strategic considerations to make employers endorse Bismarckian social insurance programmes, perceived as a lesser evil to universalist alternatives.

Preference formation and political context

The approach to preference formation adopted in this thesis is broadly informed by an “historical institutionalist” approach. Like many scholars in historical institutionalism, this thesis takes “the question of how individuals and groups define their self-interest as problematical” (Thelen and Steinmo 1992: 8) (s.a. Immergut 1998: 20). It is concerned with how the way employers, and other actors, are embedded in the political context shapes the way they understand what is best for them in a given situation. This perspective differs from a perspective that sees political behavior as determined by material interests alone. As Peter Hall critically remarks “many works in political economy explain political outcomes as a direct result of the material interests of the relevant actors defined more or less directly in terms of the economic benefits economic theory predicts will ensue” (Hall 2005: 130).

Theoretically assumed material interests do not translate directly into political action, because actors need to conduct a process of preference and strategy formation that is shaped in complex ways by the existing political context. There is often an observable gap between the material interests, as stipulated by theory, and the concrete courses of action political actors choose. The strength of material interest-based explanations is that they point us to important dimensions of conflict in politics. Their weakness lies in their lack of attention to the empirical processes by which preferences and strategies are actually formed to produce specific courses of political action. No relevant theory of preference formation can do completely without material interests, but an analytically useful understanding of preference formation also has to go beyond imputed material interests and focus on the empirical processes by which actors define and change their preferences.

Rational choice theory commonly uses a distinction between first-order preferences and lower-order preferences to incorporate the role of political interaction and external constraints into the study of political action. First-order preferences (or genuine preferences) are preferences that are understood to be exogenous to the policy-making context. They are ‘genuine’ in the sense that they are unalterable by political interaction. They are typically imputed by theory, and not identified by empirical observation. Lower-order preferences (or strategic preferences) constitute a ranking of alternative choices that actors are assumed to prefer in case their first-order preference is unattainable. Constraints emerging from the policy-making process will motivate actors to endorse lower-order preferences to allow them to influence outcomes even in situations where their first-order preference appears

unattainable. Induced by the political context, lower-order preferences may then become the publicly stated positions.

This way of conceptualizing preferences is analytically useful for capturing the importance of strategic interaction and political accommodation and it is therefore also applied in this thesis. This conceptualization is however unable, I argue, to capture fully the ways in which political context influences preferences, because this influence is not limited to strategic interaction in the policy-making process itself. The ways in which the historical political context shapes actors' stances and goals goes far beyond the importance of strategic interaction with other actors in the context of the policy-making process. The more fundamental importance of the historical political context lies in the differing types of political challenges it confronts actors with, which frames what actors consider to be meaningful choices. Often the political goals and policy stances of industrialists have been a response to challenges coming from the political sphere itself, rather than a response to problems created by the industrial production process.

To understand how actors' embeddedness in the political context influences their formation of preferences, it is useful to apply Giovanni Sartori's notion of a "ladder of abstraction" (Sartori 1984: 44-46). By ladder of abstraction Sartori means a way of ordering concepts using a dimension that ranges from a very small number of defining characteristics (a high level of abstraction) to a very large number of defining characteristics (a low level of abstraction). Different scholars use the concept of preferences at different levels of abstraction, which can create confusion about what is actually meant. By arranging different definitions of preferences according to their level of abstraction this confusion can be clarified and preferences can be linked to empirical observation.¹⁰

At the highest level of abstraction the content of preferences can be defined as universal human needs; material and immaterial ones; such as the need for food, housing, happiness, social relations, human dignity, et cetera. Preferences, understood in this way, are inscribed by human nature, or by the defining characteristics of human existence. This is a conception of preferences that underlies the classic rational choice approach to human

¹⁰ A very similar conceptualisation of interests and preferences is proposed by Woll (2008: 33-35). Woll organizes different concepts of interests along a dimension from the general to the specific, similar to as I do here, distinguishing between basic interests, role-specific interests, means preferences and policy preferences (Table 2.1). I believe that the two conceptualisations are essentially identical in their purpose, i.e. to clarify how preferences relate to historical context (Woll 2008).

behavior, embodied, for instance, in the seminal work by Gary Becker (1976). At this level of abstraction preferences are universal. They are not subject to alteration by historical context, by the cultural, economic, political or social circumstances that shape a specific period of time. However, a concept of preferences that is located at such a high level of abstraction is of low utility in political analysis because it is unable to accurately specify the content of actors' policy preferences, unless we integrate knowledge about the social and political context.

Descending the ladder of abstraction, we can define the content of preferences as general material outcomes, such as preferences to maximize income or profits, to protect property rights, or to maximize entrepreneurial freedom. To define preferences at this level of abstraction already requires that we make some assumptions about the existing economic system, about the mechanisms for the distribution of economic resources and the role positions of individuals within this system. At this level of abstraction, preferences are not universal anymore, but change with the social role of the actor. At this level of abstraction, preferences can also be preferences over specific policy outcomes, such as, for instance, higher profits or lower labor costs. But even this level of abstraction is too high to specify the positions and demands of political actors in policy-making.

To analyze preferences in the context of policy-making we need to descend the ladder of abstraction even further. If we do so, we can define preferences as *policy preferences*, as preferences over specific policy options, or "policy outputs". Preferences, understood in this way, can be preferences, for instance, over different modes of financing of a specific social policy or different institutional rules. At this level of abstraction, preferences are shaped by the political context. This the concept of preferences applied in this thesis. In other words, I refer to preferences in the sense of *policy preferences*.

The ladder of abstraction relates the concept of preferences to its different understanding by different approaches. While rational choice theory tends towards a "thin" conceptualization of preferences, operating on a high level of abstraction, historical institutionalist theory tends towards a "thick" understanding of preferences, operating on a lower level of conceptual abstraction. This means that the further we descend on the ladder of abstraction the more we need to include properties of the political and social context in order to specify the content of preferences accurately. As Steinmo and Thelen have pointed out "unless something is known about the context, broad assumptions about 'self-interested behavior' are empty" (1992: 9).

These differing conceptualizations of preferences are related to alternative understandings of preferences as being either universal or historically contingent. These two alternative understandings of preferences are not mutually exclusive or contradictory, though, as long as the two understandings are used as referring to two different levels of conceptual abstraction. Not all types of preferences are subject to contextual formation, but some are, depending on how we conceptualize the term. Preferences for such general goods as happiness or material well-being, for instance, can be assumed not to be contextually induced, but universal, while preferences over specific policy choices are induced in part also by the political context.

Descending the ladder of abstraction, making the conception of the content of preferences more specific to concrete historical situations, also links preferences to what can be termed macrofoundations. Ira Katznelson pointed out that “[m]icrobehavior...requires historical macrofoundations” (2003: 272). While the emphasis in the rational choice literature on microfoundations illuminates the way interests and preferences at the individual level shape and constrain the behavior of collective actors, the emphasis on microfoundations often neglects the impact of macrofoundations for shaping preferences and collective political action. With respect to employer associations this means that, while their policy positions will certainly be shaped, in broad strokes, by the way their members perceive their interests, they will be more than the mere aggregation of their members’ preferences. They will also be a response to the political context, which requires them to accommodate and may sometimes even define their genuine preferences. Ronald Bunn, an expert on German employer organizations, pointed out in the 1950s that:

the propaganda of an interest group serves at least a dual function. Not only is the propaganda intended to reflect the sentiments of its members but it must also attempt to influence the thinking of persons outside the group. In pursuing this second objective the propaganda of the group may sometimes contain slogans and ideals which, to a degree, are not actually shared by the members of the group. (Bunn 1959: 379)

A similar argument underpins the model of conflicting logics in collective action developed by Philip Schmitter and Wolfgang Streeck (Schmitter and Streeck 1981, 1999; see also Schneider and Grote 2005: 4-10). According to this model, employer organizations, like other interest organizations, need to balance two different logics, a “*logic of membership*”, which is governed by the values, identities and interest perceptions of the group they represent, and a “*logic of influence*”, which is governed by the properties of the political context, political institutions and characteristics of other political actors. Employer

organizations need to mediate between their members and the political target structure and, in doing so, have to try to strike a balance between the two conflicting logics. For instance, they need to be able to compromise and ensure member compliance, while at the same time they need to satisfy the preferences of their members.

Although this thesis does not try to explain the internal organizational structures and processes of employer organizations, as Schmitter and Streeck aim to, their two logics model also helps to understand employers' role in welfare state development. The two logics model can be understood as an effort to balance micro- and macrofoundations and, thereby, represents an important corrective to a microfoundational reductionism in the study of collective action. As the empirical analysis in the thesis shows, employer organizations' role in welfare state development has been shaped as much by a "logic of influence", as by a "logic of membership", though the relative importance of the two logics varied with changing historical context.

Methodology and preference analysis

To understand how political context shapes and limits the political goals and strategies of employers this thesis makes use of two specific methods: process tracing and the analysis of diachronic variation. First, a detailed *process tracing* of employers' actions and positions in specific policy reforms shows how their goals and strategies were motivated by challenges coming from the political sphere. Through the detailed analysis of the processes that led to specific policy outputs, the thesis endeavors to disentangle the complex set of causes that may have motivated employers to accept or not to accept specific policies.

The focus on timing and sequencing that process tracing allows facilitates the identification of the potentially strategic nature of political action. When, and at which point in the policy-making process, did business change its mind? Was it committed to the policy from the very start or did it come to support the policy only in the course of the policy-making process? What were the antecedents that preceded a change in position? How did employer representatives themselves justify the change? A change in position that happens in the course of the policy-making process is likely to be motivated by strategic interaction. In contrast, a position consistently taken over longer time periods is likely to reflect genuine preferences. One of the strengths of the method of process tracing is its ability to analyze questions of timing (George and Bennett 2005: 206-16; Gerring 2007: 172-85; Hall 2003: 391-5; Mahoney 2003: 363-5). Applying process tracing to the analysis of policy positions helps to identify

whether a specific position reflects a genuine preference, or a grudging acceptance in the light of unfavorable circumstances.

Secondly, the thesis relies on *diachronic variation* to analyze the importance of temporal changes in political context. Although the thesis is not an attempt to write a history of *long durée*,¹¹ it nevertheless tries to cover at least a somewhat *longer* durée than is commonly the case in the empirical study of welfare states and political economies. To analyze the relevance of broad structural factors on the way employers define their interests and preferences, we need variation in these factors. To analyze only a single policy during a very limited period of time clearly means to keep important aspects of the political context constant: the broader balance of power, the institutional setting, and the policy legacies that possibly shape the way employers perceive their interests will remain without significant change, if the analysis is limited to a short time period.

Major structural changes that have transformative effects often take the form of long-term processes and take place in a slow-moving and incremental manner, as pointed out, for instance, by Paul Pierson (2003: 181-9) and by Wolfgang Streeck (Streeck 2009: 16-21). The analysis of slow, transformative changes requires the study of long time periods. The relevance of the political rise of the labor movement and its reformist transformation, for instance, are processes that become evident only in the very long run. Equally, the changes in the broader political goals and strategies of German employers become only visible in the long-term. To understand the long-term shift by employers from a politics of pacification to a politics of containment requires attention also to the different political-economic regimes they are embedded in.

Powerful changes in political context are, however, not limited to long-term changes. They can also happen very rapidly, taking the form of a *critical juncture*, a moment in a country's history that is characterized by a high level of institutional indeterminacy and fundamental changes that may set the country on a specific path of development (see Thelen 1999: 387-8). It is especially during such moments of indeterminacy that political agency matters, as existing constraints disappear and the previous balance of power is upset (Katznelson 2003: 283-4). For this reason, the thesis focuses primarily on fundamental reforms that often happened during such critical juncture moments, rather than on the day-to-

¹¹ As done e.g. by scholars tracing modern forms of democratic governance to pre-modern structures, like Robert Putnam (1993) or Bengt Flyvbjerg (1998).

day policy-making during more settled times, when the potential for political actors to shape outcomes is more limited.

Critical junctures have asymmetric effects on the power resources of political actors. Those actors that benefited from the old order stand to lose, while those actors disadvantaged by the old order face a window of opportunity for correcting that situation. A critical juncture shifts the balance of power among political actors towards previously disadvantaged groups. In modern German history two such critical junctures have decisively shifted the balance of power from capital to labor and have compelled employers to change their strategies and attitudes towards organized labor in response. These two critical junctures were the aftermath periods of World War I and to World War II. Both events were characterized by the collapse of the old political regime. Both changed the political context of German employers drastically and made them re-evaluate their relations to organized labor. After World War I, employers lost their erstwhile ally, the Bismarckian state, and were confronted with a revolutionary challenge. The previously powerful industrialists were in a situation of political weakness that convinced them to collaborate and make concessions to labor that put the German system of industrial relations on a track towards institutionalised cooperation.

After World War II, the political clout of industrial employers was again weakened by the moral and political de-legitimization of the old order and the emergence of a new momentum for economic re-organization. This momentum was carried by the labor movement and, in part, by the Western Allies; as well as by the formation of a communist regime on east German territory. In response to these new situations, industrialists came to endorse social partnership and the notion of a “social market economy” as ways of containing programmatic challenges from a strengthened left.

These two critical junctures demarcate the three historical political-economic regimes that this thesis covers: the Wilhelmine Empire (1871-1918), the Weimar Republic (1919-1933) and the West German Federal Republic (1949-). The period of the Nazi era was excluded from the analysis, because no autonomous form of interest representation was allowed during the Nazi regime. Autonomous labor unions and employer organizations had been banned and the existing organizations dismantled by the Nazis. We do therefore not know what the positions of employer associations would have been towards specific Nazi policies, even though we know that some big industrialists had funded Hitler's rise to power

and some industry representatives had fulfilled official functions within the system of NS organizations (Hallgarten 1955; Turner 1985).

To summarize the empirical argument of this thesis, industrial employers in Germany did not accept institutions of social protection and social compromise because they wanted to create institutions that supported economic efficiency and competitiveness, but because they responded to challenges coming from the political context.¹² During the Wilhelmine period, the rise of the socialist labor movement motivated dominant groups of industrialists to support Bismarck's social insurance reforms as a tool for pacifying the working class. Their genuine preference for the maintenance of their political and economic power led them to support Bismarck's politics of social pacification. With the transformation of social democracy from a revolutionary to a reformist force and the abandoning of its more radical goals, employers' preferences for pacifying policies waned. Instead, a more pragmatic and strategically motivated acceptance of specific policy options emerged that intended to contain the expansion of social policies or dismantle disliked policy legacies by supplanting them with more favorable policies.

This thesis does not make any claims concerning the actual economic efficiency effects of labor market and social policies in Germany. The policies and institutions of the German political economy may or may not be economically efficient, but the economic efficiency benefits they potentially produce are a by-product of historical conflicts over power and authority in politics and in firms, rather than the result of deliberate institutional design. The functional efficiency of institutions cannot serve as the main component of an explanation of their origins. As Jack Knight, a scholar who uses a rational choice framework but drops the assumption of efficient institutions, notes: "institutions may or may not be socially efficient: It depends on whether or not the institutional form that favors the actors capable of asserting their strategic advantage is socially efficient" (Knight 1992: 40).

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On a theoretical level, the thesis challenges models that claim to explain business support for specific social policies solely by reference to material interests. Such models fail to take into account the extent to which policy positions are endogenous to the political context. As an alternative, this thesis suggests a perspective according to which political actors form their goals and positions in interaction with the political environment. Endogenously produced political challenges, rather than exogenously given material interests, motivated employers to accept the formation and expansion of the modern welfare state.

Summary of the main propositions

This chapter has outlined two alternative explanations for employers' acceptance of welfare state and industrial relations institutions: the cross-class coalition thesis (H1) and the political accommodation thesis (H2). The following chapters confront these two alternative explanations with the empirical evidence, whereby I intend to show that political accommodation (H2) better explains employers' role in welfare state development than economic interests (H1). Peter Hall has argued that social science advances best as a "three-cornered fight" between theory, alternative theory and empirical observations (Hall 2006: 27). Engaging in this three-cornered fight is the model that this thesis follows. Although the emphasis in the thesis is on empirical analysis, it is not intended as mere descriptive narrative. The two "theoretical corners" are pivotal building blocks for the argument of the thesis. At this point, I will thus briefly summarize these two "theoretical corners".

The cross-class coalition thesis (H1) contends that important segments of employers perceived welfare state and industrial relations policies to be in their own economic interest and therefore supported their adoption, often by deliberately forming an alliance with segments of labor. Employers' support was crucial for the adoption of these policies. Without employers' support these policies would either have been less likely to be adopted or the adopted policies would have been significantly different ones. If confirmed, this hypothesis puts into question the explanatory power of conventional labor-centred explanations. We can break down this thesis into four specific propositions:

- 1a.** Industrial employers, or a dominant segment among them, have actively supported the construction of welfare state and industrial relations policies.

1b. They did so because they considered these policies to be in their own *economic* interest. They expected benefits, in particular, in terms of skill formation and labor productivity.

1c. The preferences of the dominant segment of employers converged with the preferences of labor, resulting in the formation of cross-class alliances, issue-specific coalitions for the construction of new policies or the defense of existing ones.

1d. The primary cleavages of interest in welfare state development were sectoral cleavages. Class cleavages were of subordinate importance.

In contrast, the *political accommodation thesis* (H2), presented in this thesis, contends that employers perceived welfare state and industrial relations policies to be at odds with their economic interests, but that political constraints motivated them to accept or endorse the adoption of certain policies. Employers accepted the formation of these policies only in the context of political challenges that made the complete absence of social policy unfeasible and changed what policies employers thought to be worth aiming for. If confirmed, this thesis puts into question the causal centrality of employer interests in welfare state development and re-asserts the relevance of labor-centred and institutional explanations. We can break down this thesis into four specific propositions, which are equivalent to the propositions of the cross-class coalition thesis:

2a. The dominant segments of industrial employers were reluctant to accept the construction of welfare state and industrial relations policies.

2b. When industrial employers accepted the construction of welfare state and industrial relations policies, they did so because they perceived these policies as lesser evils. They did so (i)) because they decided to accommodate to political constraints for strategic reasons, or (ii) because political challenges led them to change their genuine preferences.

2c. Capital and labor only rarely formed alliances to promote social policies, because the genuine preferences of capital and labor often were too different.

2d. The primary cleavages of interest in welfare state development were class cleavages. Sectoral cleavages were of subordinate importance.

In addition to the two alternative theoretical positions at the center of this thesis, we can discern a third position related to employer politics. This position can be seen as a hybrid between H1 and H2 and I label it the “VoC thesis”, because it builds on the theoretical framework by Hall and Soskice (Hall and Soskice 2001). The “VoC thesis” contends that employers in coordinated market economies, irrespective of their original positions on the formation of welfare state and industrial relations policies, did over time change their positions and come to favor existing policies. This change occurred because, over time, firms adjusted their production strategies to existing institutions, thereby managing to make use of them in their own interest. Having turned institutions from constraints into resources, employers became dependent on their continuation and therefore are likely to fight for their survival (Thelen 2001: 73; Hassel 2007: 253-55; Hall and Thelen 2009: 20-1). Hall and Thelen, for instance, argue that “[i]f firms decide to support the regulatory regimes that sustain the comparative institutional advantages of the nation, it is because they also underpin the competitive advantages of the firm” (Hall and Thelen 2009: 20-1).

In this thesis, I deal with this argument only at the margins. The goal of the thesis is to explain and understand the role of employers in welfare state development, that is, their contribution to the formation of institutions that today constitute core components of the German model. To do so, the thesis focuses on those crucial moments that resulted in the formation of these institutions, rather than on the usage and day-to-day implementation of these institutions during more settled times. Nevertheless, the empirical analysis, I believe, does allow some tentative statements on the validity of the VoC thesis. I will return to this question in chapters 9 (Germany Today) and 10.V (Social Policies and Economic Accommodation).

1.IV A Preview of the Thesis

The thesis proceeds in a broadly chronological order. *Chapter two* starts with the historical origins of employer organizations in the Wilhelmine Empire. What motivated the formation of employer organizations? What was their attitude towards the emerging labor unions? The formative period of German employer associations had been the two decades around the turn of the century. In 1918, the basic organizational structure of the German system of employer organizations, as it exists today, has already been in place. The chapter shows the relationship between the emergence of labor unions and emergence of employer organization and analyzes the goals and the range of activities of the early employer organizations. The chapter shows

that employers started to organize to counter strike threats and how they developed mechanisms of coordination toward that purpose. Moreover, the chapter analyzes sectoral differences between the heavy industry and manufacturing industries in their relations to organized labor and discusses explanations for why some sectors were willing to bargain with unions, while others were not.

Chapter three analyzes the role of industrial employers in Bismarck's social reforms during the 1880s, which included the introduction of programmes for work injury insurance, health insurance, and disability and old-age pension insurance. Industry had in general supported these reforms. The chapter analyzes what motivated employers to support these reforms and how employers had tried to influence important details of the planned legislation. The chapter shows that employers had evaluated the planned social legislation primarily in terms of its political consequences, and less in terms of its consequences on labor costs and on labor productivity. The chapter shows how employers and government intended the reforms to contribute to the destruction of social democracy and the protection of business power in state and in the economy. The chapter focuses in particular on the policy of *work injury insurance*, which industry had taken a particular interest in, and shows that this interest derived primarily from the aggravation of class conflict and the existence of a problematic policy legacy in this field, rather than from the effect of work injuries on labor productivity. Moreover, the chapter critically evaluates the importance of intra-business differences in regard to the attitudes towards social insurance.

Chapter four focuses on the first critical juncture, World War I, and its domestic consequences in Germany. The chapter analyzes how the re-organization of the economy during the war and the domestic consequences of Germany's defeat and the collapse of the old regime after the war led to a sudden change in class relations and an attempt by some industrial leaders to institutionalize cross-class cooperation. The chapter analyzes what motivated these employers, who in the past had rejected any cooperation with unions, to sign an agreement with union leaders that intended to put industrial relations on an entirely new institutional basis and that involved far-reaching concessions to the union side. The chapter shows how the radically altered political circumstances and the intense political uncertainty of that moment led employers to re-evaluate their approach towards organized labor and to seek cross-class collaboration. Moreover, the chapter analyzes the reasons for the subsequent crumbling and eventual failure of the agreement.

Chapter five turns to the introduction of unemployment insurance in 1927, the most far-reaching social policy reform in the Weimar Republic. German employers had been fundamentally opposed to any form of unemployment insurance before the war, but had changed their mind after the war and eventually, after some wavering, decided to accept the introduction of unemployment insurance and cooperate in the drafting of the legislation. The chapter shows how this employer U-turn came about and what motivated it. The chapter evaluates the empirical importance of alternative motivations, including skill formation, control over the workforce and work incentives, and strategic adjustment to changing political realities. The chapter shows how an unfavorable policy legacy (unemployment assistance) had motivated employers to change their preferences with regard to unemployment insurance.

Chapters seven and eight deal with social reforms following World War II. These two chapters are preceded by a brief digression (chapter six) on how the experiences of the past, in the Weimar Republic and the Nazi regime, had induced a paradigm shift among German employers in their general relations to organized labor. Social partnership and a stronger emphasis on market competition became the new *leitmotifs* for German employer associations. This is encapsulated in their endorsement of the “social market economy” as a programmatic alternative to challenges from the left. However, while today the concept of social market economy has become almost synonymous to the welfare state, during the 1950s it meant well-nigh the opposite for German employers.

Chapter seven deals with three key social reform projects during the post-war period: the failed attempt in the late 1940s to transform the Bismarckian social insurance system into a universal and unitary insurance system; the conflict over the institutional distribution of power between capital and labor in social insurance administration; and finally, the landmark reform of the pension system in 1957, which resulted in a substantial increase in pension benefits and the automatic wage indexation of pensions. The chapter shows how employers tried to prevent far-reaching reforms that would involve higher social expenditures and a shift in power to labor. The chapter shows why employers had consistently backed the existing Bismarckian social insurance system against more egalitarian alternatives and why, at the same time, they had tried to prevent the expansion of the generosity of the Bismarckian system. Employers and their parliamentary allies had succeeded in preventing a universalist transformation of the German welfare state, but failed to prevent the “dynamisation” of pensions in the 1957 reform. The chapter shows how the character of electoral competition

had sidelined employer interests and compelled them to accommodate to the new political realities.

Chapter eight analyzes the institutionalization of firm-level codetermination in the late 1940s and early 1950s, as well as the resurgence of the conflict in the 1970s. The chapter analyzes why industrial employers had been so strongly opposed to codetermination in their firms and why the introduction of codetermination succeeded nevertheless. It shows that employers evaluated the codetermination proposals by the unions, first and foremost, in terms of their consequences on the balance of power between the two sides and in terms of control over private investments, rather than in terms of their effects on labor productivity and worker motivation. The chapter also demonstrates how the way that the unions had framed their entirely reformist goal of codetermination had evoked fears of collectivization and centralized economic planning among industrialists, which induced a strong opposition to codetermination among them.

Chapter nine analyzes the shift of German employers away from social compromise, characteristic of the post-war period, and towards a more assertive stance, which has occurred from the early 1990s on. Employers have strongly intensified their politics of containment by initiating public campaigns that promote welfare state retrenchment, policies to lower the reservation wages for the unemployed and decentralization in industrial relations. Industrial employers have become more assertive in demanding the curtailing of redistributive policies and a refocusing of social policy to its basic insurance functions. The chapter discusses the reasons for this shift, analyzing the importance of domestic and international factors in explaining why the willingness of employers to seek domestic political accommodation has declined.

Chapter ten concludes and summarizes the main themes of the thesis.

2 The Origins of Employer Associations: Coordinating against Organized Labor

“Unite firmly and unshakably. Get used to the thought that an immensely difficult battle is foisted upon you; that, in order to win it, you will have to bring enormous sacrifices and that the outcome of this battle will have to be the abolition and destruction of the social democratic ...labor unions” (Henry Axel Bueck, executive director of the Central Association of German Industry, 1911, quoted in Berg and BDI 1956: 40)

Today, the ‘German model’ of political economy is often identified with a very dense organization of private employers and a close cooperation between the organizations of capital and labor. Today, employer associations form a pillar of social partnership (see e.g. Thelen 2001; Streeck and Hassel 2003). At the time they were founded they intended to destroy and defeat the organized labor movement, as illustrated by the epigraph to this chapter. They were founded in response to the growing capacity of the labor unions to launch strikes; they were intended as anti-strike organizations. The role of German employer organizations in industrial relations today does therefore differ diametrically from the role they played during their formative years in the late 19th century. To understand this extraordinary transformation from defeating labor to cooperating with labor, and to be able to appreciate the relevance of this transformation, we need to go back to its origins.¹³

The first associations representing employer interests emerged during the period of the German Empire (1871-1918), a period of rapid industrialization and labor union growth. The most important reason for the formation of these associations was the perceived need to

¹³ A note on sources: this and the following chapter, which cover the period of the Wilhelmine Empire and World War I and its aftermath respectively, draw, among other sources, on several publications by former presidents and executive directors of German employer associations that tell the story of the evolution of their association and its politics from their personal perspective or tend to have the character of historical association chronicles. The most important ones used are by Gerhard Erdmann (Erdmann 1966b), long-time executive director of the VDA (Weimar Republic) and the BDA (Federal Republic), by Henry Axel Bueck (Bueck 1905a, 1905b), the long-time executive director of the Central Association of German Industrialists (CVDI) who was highly instrumental in the formation of German business politics during the Wilhelmine Empire, by Fritz Tänzler (Tänzler 1929, 1907), the first executive director of the VDA (National Association of German Employer Associations) after World War I, and by Ernst von Borsig (Borsig 1924), the first president of the VDA after World War I. Articles published in the two main organs of German employer associations, *Der Arbeitgeber* (founded 1910), and *Deutsche Arbeitgeberzeitung* (founded 1901) were consulted for the latter parts of the period covered in this chapter.

Scholarly publications on the historical evolution of German employer associations are relatively rare. The most authoritative and in-depth scholarly piece available has been written by the German historian Roswitha Leckebusch (Leckebusch 1966) upon which this chapter also draws. Also the work by Kessler (Kessler 1907a), an intellectual that seems to have been affiliated with the bourgeois social reform movement, and by Braun (Braun 1922) have been particularly useful.

collectively confront the challenge posed by the emerging organizations of the labor movement. As the very *raison d'être* of firms is to make profit through engaging in market competition, there is, in the context of a union-free economy, no a priori need for firms to collectively organize to represent their employer interests. The default mode of firms to achieve their preferences is individual action, not collective action. Capital can thus be expected to prefer an institutional environment that constrains entrepreneurial freedom as little as possible, in order to allow the unconstrained pursuit of entrepreneurial profit interests through the market. We can expect that this holds also for the relations of firms to the labor market, where firms can be expected to prefer to operate within the self-regulating mechanisms of demand and supply.

The formation of the first employer associations followed the formation of labor unions. While firms organized and cooperated already long before the emergence of labor unions - for instance by building price cartels or in the form of medieval guilds - the formation of *employer* organizations, as organizations representing the *employer* interests of firms, was a response to the threat posed by organized labor. I argue in this chapter that the need for employer interests to be represented collectively emerged because the entrepreneurial freedom in the labor market was threatened by organized labor. In the absence of effective labor unions there is little reason for firms to collectively represent their labor market interests. Crouch has aptly summarized this argument in the following way:

Many commentators have observed that employers have organized in response to employees, that is, that unions take the lead in the organization of the labor market; while employers find it *easier* to organize than labor, they have less *need* to do so if an individualized labor market is working well for them. Capitalists being *per definitionem* competitive, they combine only under exceptional circumstances (Crouch 1994: 334, emphasis in original).

The interaction between unions and employer associations was originally one of 'attack and defense'. The unions were attacking by raising demands, underpinned by strikes, while the employer associations were trying to ward off these demands. Early employer associations tended thus to be reactive organizations, focused on defeating strikes, but without trying to actively shape institutions and policies. One academic observer had succinctly remarked at the beginning of the 20th century that:

The labor union is everywhere the primary phenomenon, the employer association the secondary phenomenon. By its nature, the labor union attacks; the employer association fends off (...). The labor union is...primarily a strike association; the employer association an anti-strike association (Kessler 1907a: 20, translated from German by TP).

This chapter examines the formative period of employer associations in Germany, the period of the Wilhelmine Empire (1871-1918). The chapter demonstrates how employer associations during this period tried to repress and disarm the labor movement. After giving a brief overview of the political context within which the formation of employer organizations took place and the main organizations that emerged, the chapter analyzes why German industrialists decided to represent their employer interests collectively. For which purposes have employer associations been formed? What was their relationship to organized labor? Next, two key aspects of their subsequent development are analyzed: the centralization of associations and the sectoral differentiation in their relationship to organized labor. The analysis demonstrates that both processes have been a response to growing union strength.

2.I Organizational Origins in the Wilhelmine Empire

Labor unions and employer organizations both started to emerge in Germany in the course of industrialization, which gained speed quickly from about the middle of the 19th century on. Industrialization in Germany started late and was characterized very much by the features that Gerschenkron had ascribed to late industrializing countries: Technological development was fast and industrialization concentrated on large factories and large heavy industry combines (Gerschenkron 1962). With the emergence of an impoverished and politically discontent industrial working class came also the emergence of the so-called “worker question” (“Arbeiterfrage”), the concern by the authoritarian state and the industry elites regarding the revolutionary potential created by the radicalization of the working class. Initially, the response chosen by German employers was to try to destroy the labor movement by repressing its organizations. Thereby, employers could rely on the state as a firm ally.

Anti-socialist legislation: the state as a business ally

The Wilhelmine Empire rested on a political alliance between the aristocratic landowners (Junkers), heavy industry, and the army. Together they backed the newly created nation state (the *Reich*). One of the most important threats to the political stability of this regime was the socialist labor movement. The government, headed by Bismarck, tried to quell this threat by repressing the organizations of the labor movement with the so-called ‘*Anti-Socialist Laws*’ (“Sozialistengesetze”), adopted in 1878. Otto von Bismarck initiated these laws in order to curb the strength of the social democratic labor movement. For Bismarck, a conservative aristocratic landowner, the paramount objective was to secure and extend the political stability of the newly created Empire. The anti-socialist laws were passed in the Reichstag

with the votes of the conservatives and most of the national liberal deputies. The laws were ostensibly legitimated by two failed attempts to assassinate the Emperor, for which the government wrongly laid the blame on the social democrats.

The legislation effectively banned the Social Democratic Party (SPD) and organizations affiliated with the party, including the social democratic unions, from all political activities outside the Reichstag. The German Social Democratic Party (*“Sozialdemokratische Arbeiterpartei Deutschlands”*) was founded in 1875 as a merger of two competing socialist factions. The party in this early stage was revolutionary Marxist in orientation and aimed at overthrowing the existing political and economic order (Carr 1979: 140). In response to the anti-socialist legislation, the party went underground. The party continued to operate but was forced to do so from outside of Germany (Carr 1979: 140). The laws eventually failed to achieve their goal of arresting the growth of the party. The SPD managed to circumvent the laws by nominating ‘independent candidates’ and experienced a massive boost in electoral support during the 1880s.¹⁴ In view of their failure to curb the strength of the SPD, the anti-socialist legislation was finally abolished in 1890 (Lidtke 1966). Industry regretted the abolition. In 1906, the CDI executive director still insisted that ‘social democracy needs to be fought by legal means’ (CDI executive director H.A. Bueck at the CDI general assembly in Nuremberg, June 20th, 1906 quoted in Kessler 1907b: 224).

Repression of the socialist labor movement continued in various forms also after the abolition of the anti-socialist legislation, though the state became gradually more hesitant to use repression. Public employees were not allowed to join a social democratic union and employers often dismissed workers identified as union members (Raumer 1954: 426). Employers could rely on the support from the military, the police and courts to keep strikes and worker riots under control (Ullmann 1981: 203). The labor repressive policies of the state had allowed employers to ignore organized labor for some time, though this policy ultimately failed to stop the growth of the labor movement. The abolition of the anti-socialist legislation in 1890 increased the need for employers to confront organized labor on their own.

The formation of the first employer associations

As the anti-socialist legislation had temporarily diminished the need for employers to counter the labor challenge, it is likely to have had a retarding effect on the organization of employers in Germany. The two decades following the abolition of the anti-socialist legislation, from about 1890 on to the start of World War I, were characterized by a rapid growth in union

¹⁴ In 1881 the SPD received 312.000 votes, in 1890 1.4 million

strength (Schönhoven 1987: 179-210). This was also the period that became the formative years of German employer associations. Out of 154 employer associations that existed in the year 1900, 125 were founded after 1890¹⁵ (Weber 1959: 40; 1954: 98; Kessler 1907b: 239).

Before the abolition of the anti-socialist legislation, the formation of employer associations had been a relatively isolated phenomenon and remained limited to local associations covering a narrow branch of craft or industry. Associations of employers had already sporadically been formed from the 1840s on as spontaneous initiatives to ward off strikes. These groups, however, remained short-lived and were normally dismantled after the strike that caused their formation had been put down (Leckebusch 1966: 33-34).

The first permanent associations dealing specifically with employer interests started to emerge from the 1870s onwards. One of the first larger sectors to organize were the typographers, who formed their own national employer association in 1869 (*‘Deutscher Buchdruckerverein’*), in response to the formation of a national typographic worker union in 1866 (*‘Deutscher Buchdruckerverband’*). This association represented the interests of their members not only in relation to the union, but on social and economic policy issues more generally as well (Weber 1954: 100-101). In contrast to most of the employer associations to be formed in the following decades, the typographer association was prepared to negotiate collective wage agreements with its union counterpart (Erdmann 1966b: 53-54; Leckebusch 1966: 34). The vast majority of employers and employer associations in the 19th century were fundamentally opposed to any form of collective bargaining and refused to recognize unions as legitimate representatives of the workforce or as bargaining partners (Erdmann 1966b: 54).

As noted, employer organizations have historically not been the first forms of business interest groups, though they have been the first to represent the interests of firms *vis-à-vis* the working class. Already in the middle ages guilds and corporations existed in Germany to coordinate and regulate the activities of firms in the product markets and to organize vocational training. In modern times, the oldest business interest groups in Germany are the

¹⁵ In the year 1890 alone 29 employer associations were formed. The first multi-sectoral, local employer association, the association Hamburg-Altona, was formed in 1890. Its purpose was to counter mayday rallies by dismissing workers participating in them (Weber 1954: 101). In 1887, the first major nationwide sectoral employer organization was formed: the *Association of German Metalworking Industrialists* (*“Gesamtverband Deutscher Metallindustrieller”*), which is the predecessor of today’s top metalworking employer association (*“Gesamtmetall”*) (Leckebusch 1966: 36; Tänzler 1929: 12). The organization’s statutes from 1891 mentioned as the organizations goals to foster the welfare of the workers in the German metalworking industry (§ 1.1), to jointly ward off ‘unjustified plans by workers that are aiming at unilaterally dictating the working conditions and, in particular, strikes planned or organized to this purpose’ and to compensate for the damages caused by strike action (anti-strike funds) (§ 1.2) (own translation from German, quoted in Erdmann 1966: 55). These formulation of associational purposes was characteristic for many employer founded during that period.

Chambers for Industry and Commerce, which emerged in the first half of the 19th century, following the tradition of the medieval guilds. Chambers were locally based organizations with compulsory membership and carried out certain administrative tasks, such as the certification of merchants (Schulz 1961: 138). In 1861, the local chamber organizations united to form a national umbrella organization, the German Diet for Industry and Trade (DIHT) (Schroeder 2003b: 645; Braunthal 1965: 26). In addition to the chambers, trade associations had also already emerged before the formation of the first employer associations. Trade associations are associations representing the product market interests of a specific sector, in particular in relation to trade policy and economic policy more generally. In 1876, these associations decided to form their own national peak-level federation: the *Central Association of German Industry* (CDI).

The CDI: The political voice of German industry

The *Central Association of German Industry* (CDI, *Centralverband Deutscher Industrieller*) became the main organization representing the interests of German industry in the political arena. Employer associations, in contrast, played very little role in the articulation of industry's views on broader economic and social policy issues. This is for two reasons: First, the widespread formation of employer associations, as associations representing specifically the labor market interests of firms, did not occur before the abolition of the anti-socialist legislation in 1890. Secondly, the early employer associations limited their activities to defeating strikes and labor unions and did not engage in broader political debates. The CDI, together with some larger industry associations, carried out this function instead.

The CDI was founded to represent the interests of protectionist sectors in the conflict over trade policy in the 1870s. The CDI was founded as a pressure group for trade protectionism and united those sectors that were facing fierce international competition. The federation was founded in 1876 upon the initiative of the associations of the North German heavy industry¹⁶ and the Association of the South German cotton industry (Kaelble 1967: 4; Ullmann 1979: 594-595). This organization subsequently developed into the most powerful political organization of German industry during the Wilhelmine Empire and constitutes one of the predecessors of today's *Federation of German Industry* (BDI). Initially the CDI intended to be a mere pressure group in favor of a shift to protectionism.

¹⁶ The Association of the German Iron and Steel Industry (VDESI), founded 1873, and the so-called Langnam Verein, founded 1871, the full name of which was "Association for the Protection of the Common Economic Interests of Rhineland and Westphalia").

The CDI succeeded in convincing Bismarck of a shift to protectionism. An international economic crisis that began in 1873 had affected the German heavy industry particularly badly.¹⁷ In response, the heavy industry began to call for a shift in foreign trade policy from free trade¹⁸ to protectionism. A strong coalition in favor of free trade, consisting of the aristocratic landowners (the Junkers), the merchant bourgeoisie, the National Liberal Party and senior civil servants; resulted in a parliamentary defeat of the protectionists in 1875 (Lambi 1962: 62-63; Böhme 1967: 220; 1966: 389). Thereupon, in December 1875, the protectionist industries decided to unite in a new industry federation, with the purpose of lobbying more effectively for their cause and in order to seek a protectionist alliance with agriculture (Böhme 1966: 391). Under the impact of falling grain prices, agriculture eventually changed sides and turned to protectionism as well, resulting in an 'iron and rye' coalition (Lambi 1962: 67). Bismarck, motivated by plans to build an alliance with the heavy industry in order to consolidate power, eventually decided to accommodate industry with protectionist tariffs. As a result, Germany adopted a comprehensive protectionist tariffs policy in 1879, covering in particular iron and corn (Lambi 1962: 60 and 69) (Braunthal 1965: 5-6).

Having achieved its original goal, the CDI subsequently turned to representing industry's interests on broader social and economic policy issues (Ullmann 1977: 171-2). The CDI played a particularly influential role in shaping Bismarck's social insurance reforms during the 1880s (see chapter 3). Moreover, the CDI was also instrumental in the centralization of German employer associations (see below). Despite this prominent role, the CDI was, however, far from representative for the German business community as a whole and its politics was in practice dominated by the associations of the North German heavy industry¹⁹ (Leckebusch 1966: 36-37; Böhme 1967: 231). According to an estimate made by Ullmann, the CDI during the 1880s organized about 2 per cent of all German firms, which employed about one third of all German workers (Ullmann 1979: 594, and Fn47).

¹⁷ Between 1873 and 1878 prices for iron slumped by about 50 to 60 per cent (Böhme 1966: 354). Large-scale layoffs and plant closures were the consequence (Lambi 1962: 59)

¹⁸ In 1873 tariffs on pig iron, raw steel and ships had been abolished. For 1877 a repeal of further tariffs was planned (Lambi 1962: 59-60)

¹⁹ The composition of the general assembly of the CDI helps to illustrate the dominance of the heavy industry within the federation. The general assembly was made up of 300 representatives, of which 67 votes were held by the Association of German Iron and Steel Industrialists (VDESI), 38 belonged to the Rhenish-Westphalian coal mine syndicate and 10 votes belonged to the heavy industry firm Krupp. To compare, the Association of German Metal Industrialists only held 4 votes (Ullmann 1977: 176).

The manufacturing industries felt marginalized within the CDI due to the dominance of the heavy industry and did not see their positions on economic policy issues²⁰ represented well within the CDI. They decided in 1895 to form a separate peak-level federation:²¹ the *League of Industry* (BdI, *Bund der Industrie*) (Ullmann 1976; Braunthal 1965: 6). Up to 1904, these two federations dealt with a broad range of economic and social policy issues and hence served as all-purpose interest organizations for industry. In response to a major strike in 1903/1904, the proponents of a functional division of tasks won out and separate national employer federations were founded. From that time on, the two industry federations dealt predominantly with economic policy interests, while the newly created employer federations were to focus on labor market interests.

2.II Why did Employers Decide to Organize?

The main motivation for the formation of separate employer associations was to repress the organized labor movement and its demands, to prevent and defeat strikes and to collectively compensate firms for the costs of strikes. Only with the strengthening of the German labor unions and their growing capacity to organize strikes did employers start to organize as well. As shown below, the subsequent centralization of employer associations was intended to improve the effectiveness of anti-strike action. The following quote by Henry Axel Bueck, the highly influential executive director of the CDI, from the year 1890 illustrates the radical opposition of German industrialists to unions at that time:

Under no circumstances ... will German employers negotiate with the representatives of the unions ... on equal terms. Any interference of union representatives in business affairs will be firmly rejected by employers. Negotiations with the above-mentioned are rejected for now and forever. (CDI executive director Henry Axel Bueck speaking at a meeting of the Verein für Socialpolitik. Quoted in Kessler 1907a: 194 , own translation from German by TP).

The CDI, as the leading representative of German industry at that time pursued ‘class warfare from above’. Employers in Germany did not initially organize with the purpose of cooperating with organized labor, but with the purpose of destroying the latter. Initially, though, the formation of employer organizations had to overcome significant resistance from within. For various reasons, many employers considered collective action not to be expedient.

²⁰ The differences between heavy industry and manufacturing industries centred on economic policy, in particular foreign trade. While the heavy industry advocated protectionism in order to ward off cheap imports of iron, the manufacturing industries, which were benefiting from cheap iron imports did not support a comprehensive protectionist tariffs policy. Furthermore the issue of cartel protection had split these two segments of industry. The heavy industry, where cartels and syndicates were widespread demanded the legal protection of cartels, the manufacturing industries, less capable to form cartels due to smaller firms and higher fragmentation, resented cartels (Nipperdey 1961: 265) .

²¹ The association of the chemical industry left the CDI in 1883 but did not join the BdI and decided to, instead, remain unaffiliated with any of the two federations (Braunthal 1965: 6).

Some thought that employer associations would merely intensify the unwelcome class struggle, something the unions would already be looking forward to. From their view, the best way to get rid of the labor unions was not to provide them with any organizational opponent. This way, the unions would be forced to dissolve again, allowing employers to solve industrial conflicts by dealing only with their own workforce, instead of having to deal with the unions. Some also considered the conditions in their sector to be so specific that a balancing of interests within a larger association appeared not feasible to them. Others thought that they would be immune against strikes or that joining an employer association would even encourage their workers to organize or to strike (Tänzler 1929: 27; Ullmann 1981: 195).

Recognition of the necessity of collective action emerged only slowly among German employers. Collective action is only possible if a common interest is identified. Being competitors on the market, however, German employers initially had a hard time realizing that they shared common interests as employers. Instead, a competitive and particularistic mentality initially prevailed in many sectors and obstructed the formation of employer associations. One observer of the German timber industry noted in 1912 that competition in this industry was so harsh that employers were gloating if a competitor was devastated by radical union demands and strikes (Carlsson 1912: 1). To realize that such a situation is unsatisfactory and to overcome competitive mentalities was clearly a prerequisite for employer organizations to develop.

Organized anti-strike strategies: repression and coordination

To promote their central goals to defy and disarm organized labor, employer organizations developed two types of measures: first, measures to repress the labor movement in order to *prevent* strikes, and second, measures to *defeat* strikes in case they could not be avoided.²²

First, employer associations targeted measures against the labor unions as such. Employers initially perceived the socialist labor movement to be a phenomenon of temporary character, a small group of agitators that would enjoy only weak support within the working class at large. Repression was considered the most effective strategy against this movement. The simplest ways of repressing the socialist labor unions were to dismiss organized or striking workers and to hire only non-organized workers (Kessler 1907a: 143-150). Without any coordination among employers, however, workers that had been dismissed could easily

²² This subsection relies in particular upon the work by Kessler, who describes the anti-union and anti-strike measures of employer associations in detail (Kessler 1907a: 137-307)

try to find employment in a competing firm, thereby turning any sanctioning by the individual employer ineffective. German employer associations therefore developed a variety of coordination measures to sanction organized or striking workers. When recruiting new workers care was taken to avoid hiring organized workers. A basic form, which did not require employers to coordinate, was to demand that new workers declare that they do not belong to any union. More sophisticated anti-union strategies, however, were dependent on employers coordinating among each other. This section discusses the most important coordination measures used by employers.

Blacklisting. The blacklisting of organized or striking workers was one of the main forms of coordination against strikes, used in particular in the large heavy industry firms (Ullmann 1981: 199). The mining employer association (“Zechenverband”), founded 1908, for instance, banned its members from employing workers that had been found participating in strikes for a period of up to 6 months after the strike (Weber 1954: 180). In sectors dominated by smaller firms, where the administration of black lists would have been much more complicated, so-called ‘dismissal certificates’ (“Entlassungsscheine”) were used instead. These certificates were issued by the dismissing employer. They were needed by unemployed workers in order to find new employment and were used to identify organized workers. If an employer refused to issue a dismissal certificate, the dismissed worker would face difficulties finding a new job (Kessler 1907a: 143-179).

Labor exchanges. In addition, the operation of labor exchanges by the associations (“Arbeitgebernachweise”) was used to repress unionization (Ullmann 1981: 200). Employer labor exchanges were widespread in particular in small firm sectors dependent on skilled labor, like metalworking (Faust 1986: 181). They served first of all the purpose of placing workers with specific skills, but were also used to identify and reprimand striking workers (Leckebusch 1966: 123). The associations’ labor exchanges were also used to provide firms stroke against with strike-breakers. In contrast to public labor exchanges, the associations’ labor exchanges refused to place striking workers (Faust 1986: 91; Tänzler 1929: 80-83).²³

Coordinated lockouts. In addition to these preventative and repressive measures, employer associations also coordinated actions during industrial conflicts. Since the late

²³ Unions responded to the employer-run labor exchange services by establishing their own services, though these union services were rather unsuccessful because of a lack of employer cooperation. In the year 1912, 33 per cent of all job placements were mediated by the employer-run services, 36 per cent by municipal job placement services, while only 11 per cent were mediated by the union-run services. Job placement services that were run jointly by unions and employer associations accounted for only 4 per cent of job placements (Erdmann 1966b: 60).

1880s, the lockout had become the employers' main weapon (Weber 1954: 182). The coordination of lockouts was the main strategy to defeat strikes. The coordination of lockouts was intended to improve the effectiveness of the measure and reduce the costs of the lockout to the individual firm. For employers, the principal motivation to lock out workers is to inflict additional costs to the striking union by increasing the number of workers the union has to support. However, if a single employer locks out a large share of workers, this will obstruct the production process, thereby incurring a profit loss to the employer by reducing production output. A lockout only by the firm against which the strike is directed would therefore either be ineffective, if only a small share of workers is locked out, or, alternatively, would cause costly breakdowns in production, in case a larger share of workers is locked out. For employers, lockouts are therefore a double-edged sword. To confront this problem, employer associations started to coordinate lockouts. During an industrial conflict, associations distributed lockouts over the whole sector or region, involving both, firms struck against and firms not struck against (Kessler 1907a: 239-240). Through this form of employer solidarity, industrial conflict could be made more costly to the unions, while at the same time reducing the damage to the production of any single firm (Leckebusch 1966: 123; Ullmann 1981: 201).

Solidaristic employer behavior in the form of coordinated lockouts could not be achieved without compelling those firms not affected by the strike to participate in the lockout. Those firms unaffected by the strike had no material interest in participating in the lockout as compliance with the lockout meant the obstruction of production and hence a loss in profits, without giving any rewards in return. To ensure compliance by individual firms, employer associations had thus to oblige their members to follow their lockout orders (Weber 1954: 183). Such compulsion presupposed that employers generally agreed on the adequacy of coordination as a tool for defeating strikes.

Organization of strike breaker supply. The provision and allocation of strike breakers was another activity coordinated by employer associations. To provide labor to strikebound firms, associations were organizing the deployment of workers from other firms and set up strike-breaker programmes. These programmes were administrated by the associations' labor exchanges. Some of them offered jobs only to those workers who would declare to be willing to work as strike-breakers (Kessler 1907a: 218-219). Employer associations also obliged members not to dismiss strike breakers during a strike (Leckebusch 1966: 128).

Anti-strike funds. In addition to these measures intended to defeat strikes, employer associations compensated members for part of the financial costs incurred to them by strikes

and lockouts. To do so, employer associations operated their own strike insurance schemes and anti-strike funds,²⁴ which were financed by member fees (Leckebusch 1966: 123) (Ullmann 1981: 202). The creation of such compensation funds was a matter of strategic credibility for employer associations. Resolute opposition to union demands was only credible if firms could be protected from the damages resulting from industrial conflict. Without the protection offered by the strike insurance funds, individual employers would have been less likely to resist union demands in case of massive strikes.²⁵ The strike insurance funds operated by the employer associations did not provide full compensation for losses caused by industrial conflict, though. By letting the individual firm share a part of the financial risk of industrial conflict, the employer associations intended to encourage responsible behavior by firms (Tänzler 1929: 67; Erdmann 1966b: 83). Moreover, members found by the associations to pay wages substantially below sector average were excluded from compensation payments. The creation of strike insurance funds enabled German employer associations to continue their strategy of union confrontation and contributed to their ability to defy union demands for collective bargaining and protectionist labor market policies (Kessler 1907a: 289-307).

Occupational social benefits. More generally, individual employers were also trying to weaken the appeal of the labor unions by trying to tie their workforce to the firm. The main instruments to achieve this were the provision of occupational welfare benefits and the funding and promotion so-called ‘yellow unions’ (Kessler 1907a: 180-182). A wide range of occupational social benefits, such as company flats, Christmas and firm anniversary presents, and sport and amusement events, were provided to workers by many larger firms. The heavy industry firm *Krupp* maintained a particularly generous programme of occupational social benefits, a firm that had been particularly hostile to labor unions. Employers established such benefit schemes in order to weaken the appeal of the labor unions (Weber 1954: 187-191). Some firms also used occupational benefits to sanction striking workers by threatening them with the withdrawal of benefits; for instance, by canceling striking workers’ rental contract for the company flat (a specific example is documented in Weber 1954: 191).

Sponsoring company unions. Secondly, employers tried to split the working class by fostering collaborative worker organizations, the so-called ‘yellow unions’. Yellow unions were company unions (‘Werkvereine’). They were non-confrontationist and employer-

²⁴ The difference between anti-strike funds and strike-insurance schemes lies in the way benefit eligibility is determined. Anti-strike funds were providing compensation payments on the basis of discretionary decisions by the association, while strike insurance schemes involved benefit entitlements on the basis of contribution payments. Attempts to provide strike insurance services on a commercial basis failed (Tänzler 1929: 66).

²⁵ In 1906, the two newly created peak-level federations (see below) both created their own re-insurance funds for the strike compensation schemes of their member associations. In 1910, the *Verein der Arbeitgeberverbände* established a central strike insurance scheme for associations that did not have their own strike insurance fund.

dependent, they rejected strikes and collaborated with the employer.²⁶ Their political ideology was usually national-liberal or nationalist. Workers that joined a yellow union were not allowed to be a member in any other union. In the decades before World War I, some individual employers funded, and sometimes even initiated, these class-collaborationist worker organizations with the hope of gaining a political foothold within the workforce and promoting peaceful labor relations (Weber 1954: 191-193; Ullmann 1981: 202). Sometimes, eligibility for occupational social benefits was made dependent on membership in the ‘*Werkverein*’ of the firm. Financial support by the employer allowed the yellow unions to provide social benefits to their members. The yellow unions were most widespread in the large heavy industry firms,²⁷ whereas for the smaller firms in the manufacturing sectors the tending of yellow unions was less practicable (Weber 1954: 193). Support for the yellow unions was in general weak among the workers. In 1913, 85 per cent of all organized workers belonged to one of the social democratic unions, while only 3.5 per cent belonged to yellow unions, the rest being Christian unions (Kocka 1984: 66) (see chart 4.1).

Workers’ motivations for joining yellow unions were partly opportunistic. They expected material favors from their employer in return, such as occupational social benefits, while secretly remaining loyal to their political convictions. Evidence for this is found in the fact that in secret elections to appoint worker committees, yellow unions often received disproportionately weak results. Kocka, for instance, reports about an election at the union-hostile heavy industry firm *Krupp*: ‘When in March 1917 there was a secret ballot...at Krupp, a center of the ‘yellow’ movement, to elect a workers’ committee, only 4,000 out of 40,000 workers voted for the *Wirtschaftsfriedlichen*.’ (Kocka 1984: 72).

Regulating firm behavior. The coordination of anti-strike actions meant a significant tutelage of the individual employer by its association. Associations started to regulate the behavior of individual firms during strikes. In order to enforce member compliance with these rules they could rely on the control of payments from the strike insurance schemes they operated. In addition, associations also imposed fines on disobedient firms, whereby members had to pay a deposit to ensure the enforcement of fines (Suhr 1924: 14). To give some examples of how associations regulated the behavior of their members: Members were urged

²⁶ I thank user Bob C (Canada) in the internet forum of dict.leo.org for providing highly useful suggestions for how to translate the term ‘*wirtschaftsfriedlich*’ into English. Yellow unions are known in German also as “*wirtschaftsfriedliche*’ unions or ‘*Werkvereine*’. Note that the German term for unions is “*Gewerkschaften*”, and not “*Werkvereine*”, which means that in German these organizations are not called unions at all

²⁷ 27.8 % of all organized workers in the heavy industry belonged to yellow unions, according to Ullmann 1981: 200.

or obliged to include strike clauses in their supply contracts, which liberated the supplier from contractual obligations in case of a strike (Kessler 1907a: 232-237; Tänzler 1929: 63).

Also accepting ‘scrap work’ (orders a competing firm was unable to carry out due to a strike) was generally not permitted to member firms. In addition, the operation of strike-breaker programmes (see above) restricted entrepreneurial freedom as employers were obliged to temporarily hand over a number of their workers to a competitor affected by a strike, upon the association’s request. Coordinated lockouts meant that organized firms could not decide upon the usage of lockouts on their own, but had to follow the orders of their association instead. Often, member firms also had to relinquish the right to negotiate with striking workers and unions to the association, while they were, at the same time, bound to accept the outcome of the association’s negotiations (Leckebusch 1966: 125). In addition, in order to secure member solidarity during industrial conflict, firms were generally not allowed either to join or to leave an association during the occurrence of industrial conflict and had to accept notification periods of up to two years in case they intended to leave their association²⁸ (Suhr 1924: 14). In order for anti-strike coordination to be effective, employers had thus to give up part of their entrepreneurial freedom and adhere to collective discipline (Ullmann 1981: 195).

To sum up, in the 19th century German employers had developed various forms of coordination that were intended to repress organized labor, to prevent strikes and to defeat strikes. Employer associations were originally not founded for the purpose of providing an organizational basis for the collaboration with organized labor but for the purpose of excluding labor and avoiding collaboration. The majority of employer associations in the Wilhelmine Empire opposed collective bargaining. Some associations, though, started to accept collective bargaining from about 1900 on. The next section analyzes why this shift occurred.

2.III Changing Employer Strategies: Centralization and Differentiation

Between about the end of the 19th century and World War I a simultaneous process of centralization and differentiation of employer organizations took place, at the core of which was the formation of two separate national peak-level federations, which pursued partly differing strategies toward organized labor. Employer associations centralized to strengthen their power position vis-à-vis labor, while at the same time some associations in sectors where unions were particularly strong began to accommodate labor demands.

²⁸ The rules discussed here did, by and large, remain in place until as recently as the 1980s. During the 1990s, many employer associations shortened notification periods to prevent member exits.

The Crimmitschau strike: a catalyst for centralization

Not only the initial formation but also this subsequent process of centralization of employer association was motivated by the intention to better confront the challenge of organized labor. A crucial catalyst in the centralization of German employer associations was a five-month strike in 1903/04 by textile workers in the town of *Crimmitschau* in Saxony. This strike escalated into a nationwide trial of strength between capital and labor and led to the formation of the first nationwide peak-level federation of employers. The declared aim of the striking workers was to achieve the ten-hour working day and a ten per cent wage increase. The strike started in August 1903 and involved 7,000 out of a total of 8,000 workers, either as strikers or as locked-out workers (Erdmann 1966b: 66; Leckebusch 1966: 49; Tänzler 1929: 13; Beutler 1956: 31).

This strike subsequently escalated into a nationwide confrontation between capital and labor, because both sides received substantial financial support from other regions. Due to the protracted nature of the strike, local unions were running out of funds and appealed to unions in other parts of Germany for financial support. The national union organizations and the nationwide social democratic press (Weber 1954: 104), supported the strike. With the funds that they managed to collect from their allies in other parts of Germany, the Crimmitschau textile workers could prolong their strike. Similarly, the employers interpreted the conflict as a struggle over the balance of power with nationwide relevance (Schneider 1987: 220). The CDI saw the conflict as a fight ‘by the whole of German Social Democracy against the whole of the German employers about the question of power; the question whether the employer should be the master in his workplace or, instead of him, the social democratic organizations’ (CDI circular of December 24th, 1903, quoted in Ullmann 1981: 194).

The protracted nature of the conflict put the Crimmitschau employers in a difficult situation. They had to turn to the national industry federation, the CDI, for financial support. The request of both sides for help from other regions and national federations turned the conflict from a local into a national issue. Shortly after the CDI had decided to provide substantial financial support to the local employers in December 1903 the workers in Crimmitschau decided to abandon their strike unconditionally (Braun 1922: 40-41; Tänzler 1929: 15), without having wrested any concessions from the employers. The conflict ended in an unconditional defeat for labor. This show of nationwide solidarity among German employers was a result of their perception that the Crimmitschau strike was deliberately orchestrated by the socialist labor movement at the national level and part of a wider national

struggle over political power (Tänzler 1929: 14-15). The Crimmitschau employers could win this conflict only with the assistance of the CDI.

The formation of the first national employer federations

The Crimmitschau conflict motivated the organizational centralization of German employer associations. The strike made German industrialists realize their organizational weakness vis-à-vis organized labor. The Crimmitschau strike had shown to employers the increasing professionalization of the labor unions in coordinating and orchestrating strike action. Employers came to the insight that a unified national federation was needed to counterbalance the strength of the already centralized labor movement.²⁹ In January 1904, shortly after the end of the strike, the CDI took the initiative to establish a peak-level federation of German employer associations, the “Hauptstelle der Arbeitgeberverbände” (Central Office of Employer Associations). The declared purpose of the planned organization was to ward off “illegitimate union demands” and to coordinate support actions among associations during industrial conflicts (Kessler 1907b: 247). Equally important, on a political level, the centralization was also intended as a signal of flexing the muscles vis-à-vis the growing strength of the labor movement. The *Hauptstelle* declared that its formation was intended:

...not as a challenge to the workers, exacerbating the existing opposition between entrepreneurs and workers, but as a defense organization of the entrepreneurs who have been pushed into a defensive position. The Hauptstelle shall promote social peace, as long as this is possible, but it shall represent a sharp weapon, when the workers deliberately disturb peace. Most of all, it shall be a strong bulwark against the...ever growing ...claims to power of the...social democratic and union organizations (quoted in Tänzler 1929: 21)

Employers thus hoped that the new organization would re-establish the balance of power between capital and labor, which in their view had become tilted too much towards labor. The new federation was hence not merely intended to represent the interests of business but, more importantly, to shift the distribution of power between capital and labor and deter strike threats. To emphasize this point, Gustav Stresemann, the executive director of the Association of Saxonian Industrialists, declared in a speech in December 1904 ‘*we want to hope that precisely because two powers now confront each other, large strikes ... will rather be avoided than provoked.*’ (quoted in Beutler 1956: 51, translated from German by TP) (see also Leckebusch 1966: 51). Due to internal conflicts, this plan, however, eventually resulted in the formation of two rival federations.

²⁹ Attempts to form a nationwide employer federation were made previously, for instance at the CDI’s general assembly in 1890, but had failed. At that time, resistance against centralization came predominantly from the heavy industry in the Ruhr (Weber 1954: 102), where organized labor had been weak.

The committee that was set up to prepare the formation of the new peak-level federation included not only representatives of the CDI, but also its organizational rival, the *League of Industry* (BdI), which was founded in 1895 as a secession from the CDI. The CDI represented mainly the heavy industry, the BdI the smaller manufacturing industry firms (Ullmann 1976). The CDI's aspiration to align the planned federation closely with its own organization made the BdI representatives skeptical, which feared becoming overly dependent on the CDI. Talks between the two groups collapsed in April 1904 and, as a result, two separate peak-level employer federations were formed: the "Central Office of German Employer Associations" ("*Hauptstelle Deutscher Arbeitgeberverbände*"), formed by the CDI,³⁰ and the "Association of German Employer Associations" ("*Verein Deutscher Arbeitgeberverbände*"), formed by the BdI (Kessler 1907b: 248).

The formation of two rival employer federations continued the cleavage between the heavy industry, organized in the CDI, and the manufacturing and processing industries, organized in the BdI. This cleavage had emerged in the preceding decade due to conflicts over economic policy issues, in particular foreign trade and cartelization. The heavy industry was highly cartelized and sheltered by protectionism. The manufacturing industries, in contrast, tended towards free trade and market liberal positions. This cleavage also extended into the field of labor relations, as the next subsection shows. (Ullmann 1981: 198).

Irrespective of these differences, the two federations concurred in their main political purpose: to fight "illegitimate union demands" and to ward off strikes. The split between 'Hauptstelle' and 'Verein' eventually turned out as a short-lived one. Given their close affinity in purpose and activities, the two peak-level federations started to cooperate with each other soon after they were founded. In April 1913, the two peak-level federations merged into a new peak-level federation, the "Vereinigung der Deutschen Arbeitgeberverbände" (Confederation of German Employer Associations, VDA). The merger was intended to make employers more effective in their resistance to union demands and in representing employer interests more generally (Tänzler 1929: 37-38). Preventing and defeating strikes also remained the main organizational goals after the merger (Erdmann 1966b: 71).

³⁰ The close ties between CDI and "Head Office" are illustrated by the fact that both organizations were headed by the same person, Henry Axel Bueck.

Sectoral Differentiation: confrontation vs. negotiation

Although the general goals of the two peak-level federations³¹ were almost identical, both wanted to fight ‘illegitimate union demands’, their strategies differed. From around the turn of the century on, a sectoral differentiation of employer strategies in dealing with organized labor emerged. Following the abolition of the anti-socialist legislation in 1890, labor union strength experienced a boost during the 1890s, which led some sectors to rethink their relationship to organized labor. The heavy industry maintained its traditional authoritarian position, known as the ‘master in my own house’ position, while some other sectors re-evaluated their situation and decided to start to negotiate with unions. These sectoral differences are reflected in the positions of the two peak-level federations: The *Hauptstelle* was dominated mainly by the heavy industry, while the *Verein* was dominated by the manufacturing and processing industries, in particular by metalworking, construction and timber (Tänzler 1929: 16-17; Leckebusch 1966: 48-51; Ullmann 1981: 198).

The purpose of both federations ultimately was to prevent and defeat strikes, but they differed in their attitude towards collective agreements. The manufacturing industries tended to gradually shift away from the earlier confrontational approach, while the heavy industry remained adamantly opposed to organized labor and collective bargaining. The CDI and *Hauptstelle*, both dominated by the heavy industry,³² were fiercely opposed to recognizing and negotiating with unions, while the BdI and the *Verein*, dominated by manufacturing industries and construction,³³ gradually began to accept collective bargaining as, at least, one possible way of solving industrial conflicts. Construction, timber and metalworking were the main sectors that started to conclude collective agreements already before World War I, at a time when there were practically no collective agreements in the heavy industry (Kessler 1907a: 308-350; Ullmann 1977: 97-100) (see table 2.1). The smaller manufacturing firms were thus generally more prepared to recognize unions and to negotiate with them than the large heavy industry combines (Erdmann 1966b: 69; Schroeder 2003b: 646; Faust 1986: 94; Leckebusch Fn.22 on p.126 and p.129; Ullmann 1977: 178-191).

Two statements made by the BdI and the CDI respectively illustrate this difference. The executive director of the BdI, Stresemann, declared in a Reichstag meeting on April 12th, 1907:

³¹ The goals of the two federations are stated in their statutes, reprinted in (Leckebusch 1966: Appendix 4 and 5)

³² Among the associations organized in the ‘Hauptstelle’ were the associations of the iron and steel industry, mining and the textile industry, in other words, those sectors also organized in the CDI. See (Tänzler 1929: 24)

³³ Among the associations organized in the ‘Verein’ were the associations of the metalworking industry, construction, timber, as well as some craft sectors. See (Tänzler 1929: 24-25)

I hope that these collective agreements will one day become an instrument for social peace. Both sides -employers and employees - should strive with all their energy to sign such collective agreements, wherever possible. (quoted in Büren 1934: 82-83, translated by TP).

In contrast to Stresemann's view stands the official position of the CDI³⁴

The Central Association of German Industrialists [CDI] considers ...collective wage agreements between employer organizations and the organizations of the workers as extremely hazardous for the German industry and its prosperous development. Collective wage agreements remove from the individual employer the ...necessary freedom in deciding over the deployment of labor and over wage determination. Moreover, they bring the individual worker unavoidably under the control of the worker organization (...) collective wage agreements are a serious impediment to the technical and organizational progress of German industry. (CDI resolution May 5th, 1905 quoted in Schmelzer 1906: 19, translated from German by TP).

With this memorandum the CDI expressed its intention to prevent the formation of collective agreements. The CDI was determined to avoid a negotiated compromise with organized labor and, instead, hoped that industry would be able to prevail in an open power struggle with organized labor, as also the epigraph to this chapter also shows. In the view of the CDI, and with it large parts of German industry, the labor unions were functioning merely as the economic wing of the Social Democrats and were aiming at revolutionary agitation and the intensification of class struggle, rather than at concrete improvements of the living conditions of their members. Therefore, any cooperation between employers and unions would be pointless. The CDI's declared goal was to 'force down, smash and destroy the labor unions' (CDI executive director Bueck at the CDI general assembly December 1910, quoted in Schneider 1987: 221). The CDI's opposition to cooperation with organized labor is also reflected in its opposition to worker participation in the administration of social insurance via independent worker committees (see chapter 3). From the point of view of the CDI, worker committees (*Arbeiterausschüsse*) undermined the authority of management within the firm (Ullmann 1977: 172).

The position of the CDI rested on authoritarian and paternalistic beliefs about the right methods of business administration. These beliefs, known as the 'master-in-my-own-house' position, were dominant among industrialists in the Wilhelmine Empire, most notably in the heavy industry. The German historian Hartmut Kaelble has called this position 'authoritarian paternalism' (*autoritärer Patriarchalismus*). Expressing this view, CDI executive director Bueck argued that 'the worker becomes the subject of the employer with the signing of the work contract, he has to submit himself to the latter, the employer becomes his master, a

³⁴ This statement was issued in response to a decision by the Bavarian state government on March 2, 1905 to endorse the formation of collective wage agreements. The memorandum found wide support in the CDI general assembly. Only one representative, from the textiles industry, voiced objections. (Ullmann 1977: 178-9)

relationship that exists and is willingly accepted also in all other aspects of life.’ (Henry Axel Bueck, 1905. quoted in Ullmann 1977: 179). As Kaelble emphasizes the dominance of these authoritarian-paternalist beliefs among German industrialists destroyed the basis for any cross-class collaboration in Wilhelmine Germany (Kaelble 1967: 56-60).

The first larger sectors that started to deviate from the ‘master in my own house’ position were construction, printing and timber³⁵ (see table 2.1) (Kessler 1907a: 319-323; Ullmann 1977: 97-100). These sectors belonged to the *League of Industry* (BdI), which organized those sectors that were discontent with the CDI and its policies. In the construction sector the first local collective agreement was signed in 1899 (Cologne). In 1910, construction employers launched an initiative for a nationwide collective agreement in this sector, in response to a large strike of construction workers in the same year (Erdmann 1966b: 77). The construction sector was characterized by very small firms. Fierce price competition had put pressure on firms to undercut the wages paid by competitors. The construction employer association (‘Arbeitgeberbund für das deutsche Baugewerbe’) intended to harmonize wages through a nationwide collective agreement, in order to stop destructive price-cum-wage competition (Tänzler 1929: 59-60; see also Markovits 1986: 33).

The problem of competition from firms paying substandard wages affected in particular sectors dominated by small firms and unskilled labor. While in the heavy industry the challenge of price-cum-wage competition was neutralized by the formation of price cartels and production syndicates,³⁶ the dominance of smaller firms in construction made the option of price cartels unrealistic in this sector, because compliance was difficult to control given the large number of competitors. Compliance with collective wage agreements, by comparison, appears to have been easier to control because workers and their unions could be relied upon to demand the compliance by the individual firm. For the construction sector, the harmonization of wages served thus as a functional equivalent to the formation of a prize cartel (Tänzler 1929: 60-61; Schönhoven 1987: 223). Employers in this sector, hence, did indeed see the advantages of collective agreements and used them to restrict downward wage and price competition.

In general, however, collective agreements were not a widespread phenomenon in the period before World War I. In 1914, only about 16 per cent of all German workers were

³⁵ The first sector to sign a collective agreement were the typographers (1873). Their example did however remain without followers for more than two decades. The construction industry followed with first agreements signed 1899 (Berlin) and 1903/04 (Cologne). (Erdmann 1966b: 77) (Kessler 1907a: 21-22)

³⁶ While the price cartels and production syndicates in the heavy industry had resulted in an extent of market dominance that allowed these firms to coordinate effectively against strikes, the smaller firms predominant in construction and manufacturing were far more vulnerable to strikes.

covered by a collective agreement (see table 2.1 below). In addition to construction, collective agreements concentrated in the sectors of clothing, food, metalworking, printing and timber. As table 2.1 shows, collective agreements were almost absent in the heavy industry before World War I (Tänzler 1929: 71; Ullmann 1977: 97-100). Coverage by collective agreements also varied according to firm size. Most workers covered by collective agreements were employed in small- and medium sized firms (<100 workers). Larger firms were less prepared to subject themselves to collective agreements. In 1914, only about 14 per cent of all covered workers were employed in firms with more than 100 workers (see table 2.2 below). This reflects the opposition to collective agreements in the heavy industry and other “big industry” sectors (textiles, chemicals).

Explaining sectoral differences

Why did the initiative for collective bargaining come from the small and medium-sized firms in sectors like construction and not from the large firms in the heavy industry? How can these differences in strategy regarding organized labor be explained? The willingness of the small firm sectors to negotiate with organized labor and accommodate labor demands is most likely the result of the fact that these firms were more vulnerable to industrial conflict. The smaller firms that characterized the manufacturing and processing industries were less well equipped to resist union demands compared to the larger firms in the heavy industry, and therefore were more willing to cooperate with organized labor.

Table 2.1 Collective bargaining coverage acc. to sector (1914)

Sector	Absolute Number of workers covered	Percentage of workers covered
Agriculture	3 490	4.3
Heavy industry	92	0.0
Stone and earth industry	60 166	8.7
Metalworking and machine building	147 503	9.0
Chemical engineering	7 154	5.3
Textiles	10 874	1.3
Paper	38 844	20.1
Leather	32 254	22.8

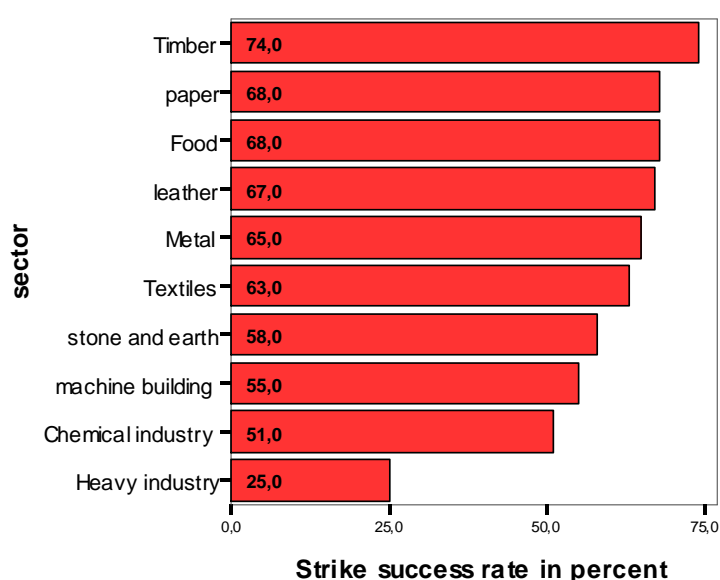
Timber	163 597	31.1
Food	108 237	14.1
Clothing	148 857	22.9
Construction	474 824	46.8
Printing	88 448	52.7
Commerce	45 165	4.5
Transport	53 919	19.7
Hotels and restaurants	7 600	2.6
Music and theatre	559	0.3
Others	4 167	5.5
Total	1 395 723	15.8

Sources: Tables 5 and 7 in Ullmann 1977: 225-228 . The percentage of workers covered has been calculated on the basis of the total number of workers in 1907. The percentages thus serve only as an approximation.

Table 2.2 Collective bargaining coverage acc. to firm size (1914)

Firm size (no. of employees)	<5	6-10	11-20	21-50	51-100	101-200	>200	All firms
Percentage of all workers covered	14.3	17.9	18.8	25.6	8.8	6.5	7.8	100

Source: Table 8 in Ullmann 1977: 230.

Chart 2.1 Strike success rate according to sector (1907-1914)

Note: share of strikes in which unions succeeded to wrest concessions from employers, 1907-1914 (Kaelble 1967: 70, Fn119)

As shown in chart 2.1 above, the ability of labor unions to wrest concessions from employers through strike action differed markedly across sectors. Within heavy industry, the unions were much weaker compared to the manufacturing and processing industries. Only 25 per cent of all strikes in the heavy industry yielded concessions from employers. The existence of large cartels and production syndicates in the heavy industry allowed these firms to coordinate effectively against strikes, for instance by blacklisting organized workers and coordinating lockouts.³⁷ In addition, the regional concentration of the heavy industry in the Ruhr area and the very small number of employers in this sector facilitated the coordination

³⁷ The coalmines in the Ruhr also formed their own employer association relatively late, in 1908. The need for an own employer organization was perceived as low in this sector (Faust 1986: 94).

among employers, while, at the same time, made it more difficult for workers to exercise bargaining power by threatening to change employer. The very large firms in this sector (see table 2.3 below) were least vulnerable to threats from organized labor and hence were able to hold on to their traditional ‘master in my own house’ position more so than other sectors. Up to 1918, there were practically no collective agreements in the heavy industry. The heavy industry was also the sector that was able to rely most extensively on blacklisting, occupational social benefits and on the funding of yellow unions as measures of union repression (Faust 1986: 92; Ullmann 1981: 203; see also Markovits 1986: 33).

Table 2.3 Share of very large firms according to sector

SECTOR	1882	1895	1907	Note: Workers employed by firms with more than 1000 employees as a percentage of all workers employed in the sector. Heavy industry defined as mining, iron, and steel. The category metal processing excludes locksmiths and plumbers, NA: data not available
Heavy Industry	34	45	53	
Stone and earth	2	3	3	Source: Sombart 1921 (Appendix 22 on p.506-507)
Metal processing	0.5	4	7	
Machine building	8	10	17	
Electro-technical industry	NA	33	40	
Chemical industry	5	13	18	
Textiles	2	4	4	
Paper	NA	2	2	
Food	5	3	8	
Construction	1	2	2	
Printing	NA	1	2	

In the manufacturing and processing industries, in contrast, the ‘master in my own house’ approach became less viable over time. Unions in these sectors were in general much stronger and the smaller firms in this sector were more vulnerable to strikes (Faust 1986: 100; Ullmann 1981: 203). Between 51 and 74 per cent of strikes in these sectors resulted in concessions by employers, as shown in chart 2.1 above. As they faced strong unions, employers in these sectors also had to be more prepared to negotiate with unions. They were more willing to accommodate labor demands because they were more dependent on the goodwill of organized labor. The timber industry, the sector suffering heaviest from strikes, was also among the first to sign collective agreements with their union counterpart. To

simplify, where unions remained weak, employers remained hostile to cooperation, where unions were strong, employers eventually decided to cooperate.

In short, the sectoral variation in the willingness of employers to negotiate with labor unions and conclude collective bargains before World War I was the result of sectoral differences in the ability to resist strikes by way of confrontation and repression. Where unions were weak and firm size was large, as in the heavy industry, employers could continue the traditional authoritarian approach to industrial relations, described in section II of this chapter. Where unions were growing stronger and firm size was comparatively small, the authoritarian approach became unsustainable and employers needed to show more flexibility in dealing with labor demands.³⁸

A different explanation is offered by the skill formation thesis, which suggests that the willingness of employers to accommodate labor results from their dependence on workers with specific skills. Collective wage agreements offer income security and, hence, result in a protection of skill investments (Estévez-Abe et al. 2001: 180-181; Cusack et al. 2007: 388). Unfortunately precise and reliable statistical data on sectoral skill structure are not available for that period. We have to rely on general knowledge on the skill profiles of different sectors instead. In general, the heavy industry relied mainly on unskilled labor, while the manufacturing industries tended to rely more on skilled labor. This fact provides some plausibility to the skill formation thesis, as the heavy industry (coal mines, iron and steel) was the sector most hostile to collective bargaining. However, the two largest sectors concluding collective bargains already before World War I, construction and timber, were also relying mainly on unskilled labor. Both sectors were suffering from widespread strike action during that time (see above) and were unable to coordinate effectively against strikes due to small firm size and intense competition in these sectors. In these sectors, employers needed to be flexible in dealing with organized labor and gradually turned to collective bargaining as an alternative to repression and authoritarianism.

Conclusions

Employer associations are today an organizational pillar of coordinated capitalism in Germany. This chapter has analyzed the historical origins of employer coordination. What

³⁸ Swenson 1989: 41 provides another alternative explanation, which centres on the extent of exposure to international competition. According to his explanation, sectors highly vulnerable to international competition were more open to collective wage bargaining compared to sheltered sectors. This explanation is disconfirmed by the fact that, since 1879, the heavy industry was shielded from international competition by protective tariffs. Protectionism did not prevent the heavy industry from opposing collective bargaining.

motivated firms to form employer associations? Why did firms perceive a need to represent their labor market interests collectively? The chapter has shown that confronting organized labor more effectively was the main motivation for the formation of employer associations in the Wilhelmine Empire. The formation of employer associations was, first and foremost, intended to prevent and defeat strikes and to repress the labor movement with various measures, rather than at forming an organizational basis for the cooperation with labor. German industrialists considered the labor unions and social democracy as revolutionary threats to the established political-economic order. A 'master in my own house' approach to labor relations dominated German industry. Coordinated lockouts, strike breaker programmes, blacklisting of striking workers, anti-strike funds, the funding of house-broken 'yellow unions' and occupational social benefits were characteristic measures of employer associations and individual employers to defeat strikes and destroy organized labor.

In their confrontationist approach to organized labor German industrialists during that time could count on the state as their firm ally. The anti-socialist laws had assisted industrialists to keep the socialist labor movement in check. The abolition of these laws in 1890 had required employers to rely increasingly on their own organizational capacities to confront the socialist labor movement. The formative period of German employer associations was the period following the abolition of the anti-socialist laws, a period characterized also by growing union strength. The historical formation of employer associations was a response to a political challenge, the rising labor movement, rather than the result of any objective economic necessity for organization. Also the centralization of employers' organizational structure was intended to improve their effectiveness in countering the labor challenge.

The chapter has shown that the vast majority of employer associations in the Wilhelmine Empire refused to recognize unions or to negotiate with them. They intended to destroy the labor movement, not to integrate it by institutionalized cooperation. Only from about the turn of the century onwards did some sectors start to conclude collective agreements, most notably construction and timber. In contrast, the leading heavy industry sector remained adamantly opposed to any form of cooperation or bargaining with unions until World War I. Based on sectoral comparison, the chapter has demonstrated that the variation in the willingness of German employers to conclude collective agreements is most likely the result of sectoral differences in union strength. The smaller firms in the manufacturing sectors were more vulnerable to strikes than the larger firms in the heavy industry and thus were unable to afford the authoritarian approach to labor relations pursued

by the heavy industrialists. They needed to take a more flexible approach and try to accommodate labor demands. The origins of employer associations and collective bargaining are thus closely linked to union strength.

Few things about the historical evolution of industrial relations in Germany are as puzzling as the enormous change that they have gone through since the beginning of industrialization. Today, German employers prefer strong unions, which are able to enforce collective agreements and industrial peace. German employers do, in principle, endorse social partnership and social compromise. Employers did, however, not pursue this strategy from the very beginning. Originally, employers were highly reluctant to accommodate labor. The shift from confrontation to accommodation occurred only gradually over time. Accommodation occurred as the result of a series of political struggles that took place at critical junctures in German history against a background of far-reaching changes in the political and economic context. These struggles and changes are analyzed throughout this thesis, in particular in the chapters 4, 6 and 8.

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Defeating the socialist labor movement was a goal German industrialists shared with the Bismarckian government and state elite. Rather than relying on repressive measures exclusively, social policy was instrumentalized for this goal as well. During the 1880s, the German Empire had introduced public social insurance programmes to protect workers against the risks of work injury, sickness, old age, and disability. The German heavy industry and the CDI had broadly supported these plans and, in the case of work injury insurance, even acted as an active promoter of a public policy solution. As this chapter has shown the heavy industry was the sector most resolutely determined to destroy the socialist labor movement. The next chapter will look at the involvement of German industry in Bismarck's social insurance reforms.

3 Bismarck's Social Reforms: German Employers and Social Pacification

With the Bismarckian social reforms in the 1880s, Germany had become the first country in the world to introduce a public system of social insurance. By and large, these reforms were supported or accepted by the leading interest associations of German industry. Looking back, Henry Axel Bueck, the executive director of the immensely powerful *Central Association of German Industry* (CDI), had praised these reforms 'as a work of civilization of the highest order, which, as a model for all times, will bring [the Empire] honor for good' (Bueck 1905a: 792). Why did the powerful heavy industrialists organized in the CDI decide to back social reform? As we have seen in the previous chapter the CDI adamantly refused to cooperate or negotiate with organized labor and considered the ideas of social democracy as an eminent threat to industry and its interests. The CDI's motivation was thus not to forge an alliance with the organizations of the labor movement. Why did the CDI thus decide to support a policy that apparently aided the economic independence of the working class?³⁹

To answer this question will not only allow us to understand the role industry has played in the formation of the German welfare state but will also contribute to our understanding of the more general question of what shapes the positions that industry takes in politics. The conventional labor mobilization approach attributes the formation and expansion of the welfare state to a decline in capitalist power. According to this view, employers have been compelled by the strength of the labor movement to accept the welfare state. In contrast, the cross class coalition approach attributes the formation and expansion of the welfare state to the structural power of employers, who perceived the welfare state as being in their own economic interest. The analysis in this chapter therefore pays particular attention to the importance of economic self-interests and coercion by political constraints.

After presenting the political context and the goals of the government (section I), the chapter analyzes the positions of industrial employers concerning the three social insurance programmes, whereby the analysis focuses on the programme of work injury insurance (II), because this is the programme that industry was most interested in. Industry paid somewhat

³⁹ Note on sources: This section uses archival documents contained in a multi-volume collection of primary sources published by the Historical Commission of the German Academy of Science in Mainz (Ayass et al. 1998, 2001; Ayass et al. 2003; Tennstedt et al. 1995).

I also draw on the PhD thesis by Monika Breger on the role of industry in the design of Bismarck's social policy, (Breger 1994, 1982), the PhD thesis by Heinrich Büren (Büren 1934) and the work of Hans-Peter Ullmann, (Ullmann 1979). For the analysis of intra-business differences I draw on a report by the Royal Prussian Statistical Office, (Francke 1881).

less attention to the issues of health insurance and disability and old-age pensions (III). After evaluating the relevance of intra-business differences (IV), the chapter finally discusses the main motivation of industry for supporting the introduction of social insurance (V).

3.I Social Insurance as Social Pacification: The Main Actors and their Goals

The origins of the German welfare state are to be found in the response by the conservative state elites to the challenges created by the so-called ‘social question’ (*‘soziale Frage’*). The so-called ‘social question’ stands for the concern by the government and economic elites about how to pacify the politically radicalized working class and how to secure the political stability of the authoritarian political regime. The founding of the German nation state in 1871 was initially followed by a short economic boom, but was followed by a severe international economic recession that started in 1873 and led to falling world market prices for German products and soaring unemployment in Germany⁴⁰ (Kitchen 1978: 139f.). The crisis had raised the anxiety of the political and economic elite about the revolutionary potential of the increasingly discontent and radicalized working class (Ritter 1983: 9). The Paris Commune 1871, the short-lived revolutionary municipal government of Paris, had further contributed to the anxiety of the government and economic elites about a potential spill-over of the revolutionary moment to Germany.

In this context, Bismarck responded with a political strategy that became known as *innere Reichsgründung*,⁴¹ or, the domestic political consolidation of the Empire. This strategy resembled a Machiavellian approach of securing the political loyalty of important social groups by handing out concessions, while at the same time repressing political opponents. The introduction of social insurance, like many other of Bismarck’s policy decisions, was less motivated by a commitment to deal with specific policy problems, but by the expectation that the reform would shore up popular support for the Empire. The introduction of social insurance was an integral part of a ‘double strategy’, a strategy of divide and conquer, or of “carrots and sticks” (Ritter 1983: 28-29).

The suppression of the socialist labor movement through anti-socialist legislation was the other part of the strategy. As mentioned in chapter 2, these laws were introduced in 1878 with the support of most of the Conservative and National Liberal deputies in the *Reichstag* and banned the organizations of social democracy of all political activities. These laws were passed in response to an assassination attempt on the Emperor, for which the government put

⁴⁰ The depression was triggered off in the USA by a stock market crash and bankruptcies in the railway sector (Kitchen 1978: 139ff)

⁴¹ The term ‘innere Reichsgründung’ was coined by the German historian Böhme (Böhme 1971).

the blame on the social democrats. The laws were abolished in 1890, because of their perceived ineffectiveness in weakening the social democrats. Following their abolition, the parliamentary strength of the Social Democrats soared (see table 3.1 below).

Table 3.1 Distribution of Reichstag seats in the German Empire (1871-1918) in percent

Party groups/ Election	1871	1874	1877	1878	1881	1884	1887	1890	1893	1898	1903	1907	1912
Conservative Parties	24.6	13.8	19.7	29.3	19.7	26.7	30.5	23.4	25.2	19.9	18.9	21.1	14.3
National Liberals and smaller right-wing liberal lists	40.6	39.8	35.5	27.4	11.9	12.8	24.9	10.6	13.4	11.6	12.8	13.6	11.3
Liberal Union (centrist)	0	0	0	0	11.6	0	0	0	3.3	3	2.3	3.5	0
Left-wing liberals	12.3	12.6	9.8	7.3	17.4	18.7	8.1	19.1	8.8	9.3	6.8	8.9	10.6
Centre Party (Catholic)	16.5	22.9	23.4	23.7	25.2	24.9	24.7	26.7	24.2	25.7	25.2	26.4	22.9
Socialist Labor Party (incl. predecessors)	0.5	2.3	3	2.3	3	6	2.8	8.8	11.1	14.1	20.4	10.8	27.7
Others	5.5	7.6	8.6	10.2	11.3	10.9	9.2	11.4	14.3	16.5	13.7	15.7	13.1
Total	100	100	100	100	100	100	100	100	100	100	100	100	100

Legend: Conservative Parties: German Conservative Party + German Reichspartei. Right-wing liberals: National liberals+ Liberal Reichspartei, Left-wing liberals: German Progress Party + German People's Party

Source Wikipedia <http://de.wikipedia.org/wiki/Reichstagswahl>

The introduction of 'worker insurance' was the 'carrot part' of Bismarck's strategy. A speech delivered by the Emperor Wilhelm I on November 17th, 1881, the so-called 'Imperial Message', announced the government's plans for the introduction of social insurance:

...the healing of the social damage cannot be achieved exclusively by way of repression of the social democratic riots, but equally needs to involve the positive promotion of the welfare of the worker (Imperial Message, 1881 November 17th Ayass et al. 2003: Document No. 9, 61-64).

Bismarck himself expressed the objectives of his social policy plans in a similar way:

If there would be no Social Democrats, and if not so many would be afraid of them, then not even the moderate progress that we have made so far in social reform would exist (Bismarck in a speech to the Reichstag, 1884 November 26th, quoted in Hentschel 1983: 9).

The genesis of the welfare state in Germany was not the result of a political project pursued by organized labor or social democrats, but, to the contrary, a part of a conservative, authoritarian project to keep the social democrats away from power. Social insurance was the

project of the governing state elite aimed at consolidating its hold to power. German Social Democracy at that time was orthodox Marxist in its ideological orientation and aimed at overthrowing the capitalist order through a socialist revolution (Berman 2006: 35-36). The government offered material benefits to the working class in order to keep it away from political power. In the absence of a radical socialist movement the introduction of social insurance at that time would most likely not have happened. The growing strength of the socialist labor movement and its orthodox Marxist orientation were the ultimate motivation for the government to seek the introduction of social insurance. In the absence of a radical socialist labor movement, an authoritarian political regime would have been unlikely to embrace the welfare of workers. In addition to this, intellectual input coming from bourgeois social reformers had a remarkable influence on the thinking of the state bureaucracy.

The role of the 'bourgeois social reformers'

The so-called 'bourgeois social reformers' served as a catalyst for the genesis of social policy in Germany. They functioned as intellectual agenda-setters. The bourgeois social reform movement consisted of academics, economists, journalists as well as some renegade industrialists. The goal of the movement was to find a solution to the 'social question', that is, of how to conciliate and pacify the working class. These so-called 'socialists of the chair' ('*Kathedersozialisten*'), had a particularly strong impact on the thinking of government officials and industrial elites. They sensitized the latter groups towards social problems and often proposed very elaborate and detailed policy solutions. Their activities consisted of problem-oriented studies, lectures, speeches, publications, and educational activities. The bourgeois social reformers rejected the economic laissez faire liberalism of the Manchester School. They advocated state-interventionism to secure the loyalty of the working class to the political regime. They also advocated the introduction of social insurance, worker protection laws and worker participation in economic affairs through works councils and corporatist institutions. Finally, they influenced the genesis of social policy, first, by permanently confronting the political and business elites with social problems and, secondly, by providing detailed policy proposals that state officials could draw upon (Plessen 1975 presents a detailed analysis of the political impact of the social reformers).

The movement found its first expression in 1844 with the foundation of the 'Central Association for the Welfare of the Working Classes' ('*Central-Verein für das Wohl der arbeitenden Klassen*'). The association was made up of senior state officials and business people and aimed at improving the living conditions of workers. The association made remarkable proposals concerning labor relations, which were in strong contrast to the 'master-

in-my-own-house' attitude prevailing among German industrialists at that time. The group demanded equal representation of workers and employers in the business chambers and business courts. To avoid arbitrary decisions by employers, it demanded that employers be obliged to draft shop rules detailing, *inter alia*, dismissal protection and working time regulations. In general, employers responded to these proposals with hostility. In 1849, the government rejected a detailed draft law for shop rules presented by the association, with the argument that this would violate entrepreneurial prerogatives and that these issues should be left to the individual employer to decide (Leckebusch 1966: 19-20).

The most influential organization of the movement was the 'Association for Social Policy' ('*Verein für Socialpolitik*'), founded in 1872 by a group of influential political economists⁴² with the purpose of contributing to 'the enlightenment of the public opinion in favor of a social reform' (Schönberg 1886: 23). Among its members were also senior government officials, politicians from bourgeois parties, journalists and industrialists. The association pursued its goals by organizing political debates and conferences, carrying out problem-centred policy analysis and disseminating its studies and policy proposals through writings and lectures. The group's protagonists criticized the individualizing tendencies of industrial capitalism as well as laissez-faire liberalism and advocated state interventions to solve the 'social question'. '*The deep cleavage that runs through our society*' declared Professor *Schmoller*, one of the original members of the association in his inaugural address in October 1872:

the struggle which today separates entrepreneur and worker, the classes which have and those which have not, the possible threat of a...looming social revolution, have....created doubts, whether the prevalent economic doctrine will maintain its dominance,...History teaches us that all higher cultures... have collapsed because of... social class struggles and revolutions, their incapacity to find a reconciliation between the upper and the lower classes ...The ideal should be nothing less than to allow an ever larger part of our people to participate in all higher goods of culture, education and prosperity (inaugural address by Schmoller at the 'Eisenach conference', October 8th, 1872, quoted in Erdmann 1966b: 61-62)

The bourgeois social reformers have contributed substantially to the genesis of the German welfare state. Many of its protagonists enjoyed good contacts with the state bureaucracy and confronted state officials and industrialists with social problems and reform proposals. They offered an intellectual blueprint for a reformist solution to the 'social question.' It is notable how many of the proposals that first emerged among the social reformers were really implemented in Germany later on: social insurance for workers, worker

⁴² Among the founding members were the university professors Brentano, Schmoller, Schönberg, Wagner, Sombart and Weber (Leckebusch 1966: 21-22).

protection laws and institutions for the participation of the working class in economic decision-making, in particular through works councils (Parnell 1994: 158 re social insurance and 206-207 re works councils; see also Plessen 1975).

Despite their apparent impact on policy making, the social reformers did in general not stand in high esteem, neither with industrialists nor with the socialist labor movement. For different reasons, both kept a sharp eye over the bourgeois social reformers. Industrialists appear to have been generally uneasy about the reform proposals. In general, the social reform proposals were perceived by industry as being somewhat unrealistic and as too much of a burden to firms. The executive director of the CDI, Henry Axel Bueck, remarked in 1906 that ‘every industrialist will think twice about hiring a young graduate who enjoyed his social policy education at the Berlin Business School under Professor Sombart’ (quoted in Kessler 1907a: 43, translated from German by TP. Sombart was one of the original members of the Verein für Socialpolitik). The social democrats were equally critical of the social reformers. They accused the social reformers of being submissive to the interests of the existing political regime and defending ‘capitalist class rule’. Not without any reason, the Social Democrats perceived the social reform movement as an attempt to pacify the working class and to consolidate the capitalist economic order (Osthold 1934: 13-14).

The role of social democracy

The socialist labor movement refused to cooperate in the social insurance project because they sensed the ulterior motives behind it. *Der Sozialdemokrat*, the SPD’s official organ,⁴³ reported in November 1881 that two party leaders had been approached by conservative politicians offering the following bargain: If the social democrats would accept to support social insurance reforms, these parliamentarians would vote in favor of abolishing the anti-socialist legislation and would call on their party colleagues to vote for the social democrats in some constituencies in Berlin. The social democrats rejected the offer (*Der Sozialdemokrat* No.48, 1881, November 24th, Document No. 21 in Ayass et al. 2003: 85-88). The social democrats were not in principle opposed to social protection, though, and had at other occasions already demanded worker insurance. They perceived the government’s social policy plans as an attempt to placate the working class and to avert more far-reaching reforms. In the same article in *Der Sozialdemokrat* this position was justified as follows:

May our persecution be increased tenfold, we will never give our approval to such ‘reforms.’
Under no circumstances will we relinquish the right of the people to work and to exist, the right

⁴³ “*Der Sozialdemokrat. Zentralorgan der deutschen Sozialdemokratie*” was the official organ of the German Social Democrats. It was published in Zurich to circumvent the anti-socialist legislation. Since 1881, its chief editor was Eduard Bernstein (Ayass et al. 2003: 85, Fn1).

and the obligation of the people to achieve its demands, if necessary through violence, for the lentil dish of a work injury and disability insurance of most dubious value. This is the proud answer of Social Democracy to the Imperial Message. (*Der Sozialdemokrat*, No.48, 1881 November 24th, reprinted as document no. 21 in Ayass et al. 2003: here 88, translated by TP).

Similarly, the SPD party congress in Copenhagen⁴⁴ 1883 declared that it considered the ‘so-called social reforms’ a red herring that would be ‘used only as a tactic tool, to distract the workers from the true path’ (resolution of the Congress of the German Social Democratic Party in Copenhagen, 1883 April 1st, reprinted as document No. 34 in Ayass et al. 2003: 127). Social democracy did thus not support Bismarck’s plans and did not participate in the drafting of the legislation.

The role of industrial employers

Industry did not initiate the social insurance reforms, but went along with the government’s plans primarily because it acknowledged the need to pacify the working class. Politically, industrial employers were affiliated with the conservative parties and the National Liberal Party (see table 3.2 below), whereby a split developed between the dominant heavy industry and the small, but growing, manufacturing industries. The heavy industrialists, like the agrarian industrialists, aligned themselves with the two conservative parties (*Reichspartei* & Conservative Party). They viewed the labor movement as a revolutionary threat and rejected any cooperation with its representatives. The manufacturing industries aligned themselves with the National Liberal Party and, facing strong unions in their sectors, were more open towards labor demands, as shown in chapter 2 (see also Kaelble 1967: 109-11).

Both groups did, in principle, support Bismarck’s social reform project, though the heavy industry took a much more active role in the reform process (Ullmann 1979: 588-90). With the CDI, the heavy industry had a powerful political organ and enjoyed privileged access to Bismarck. Its strong antipathy against the social democratic labor movement provided it with a particular interest in the suppression of the latter. The attention of the heavy industry focused in particular on the issue of work injury insurance, which the heavy industry actively promoted, while the programmes for health, disability and old-age insurance received far less attention from the heavy industry, as well as other sectors (Breger 1994: 38).

⁴⁴ To circumvent the anti-socialist legislation the Congress had to be held abroad.

Table 3.2 Industry representatives in the German Reichstag (1890-1918)

Party	Total number of Reichstag deputies	...of which industrialists	Share of industrialists in %
Conservatives	358	28	7.8
Dt. Reichspartei (German Imperial Party)	130	32	24.6
Centre	600	37	6.1
National Liberals	291	94	32.3
Left-wing Liberals	300	43	14.3
Social Democrats	369	10	2.7

Note: data aggregated over the 8th to 13th legislative period ,excludes smaller parties. Source: Jaeger 1967: 51, Table 3 and table 6, own calculations

What motivated industrial employers to endorse Bismarck's social legislation? Were employers' intentions identical to those of the government or did employers support the government's plans for different reasons? What were the demands articulated by employers? Did the reforms live up to industry's expectations? How widespread was support for social insurance within industry? The following two sections analyze in detail the intentions of industry, the goals industry intended to achieve, and what kind of social policy industry wanted. Section II deals with the case of work injury insurance, the programme that industry had paid the greatest attention to. Section III deals with the programmes of health, disability and old-age insurance, while section IV discusses the relevance of intra-business differences.

3.II Employers' Support for Work Injury Insurance

The attention of industry centered primarily on the issue of work injury insurance. The CDI and the associations representing heavy industry⁴⁵ supported the introduction of a public work injury insurance with compulsory coverage for all workers. Industry was one of the agenda-setters on the issue of work injury insurance, which contrasts with the comparatively passive role of industry on other social policy reforms. A draft bill developed by a group of heavy industrialists led by *Louis Baare* substantially influenced the government's own draft bill (Breger 1994). The case of work injury insurance is one of the extremely rare cases where

⁴⁵ The associations representing the heavy industry were in particular the Association of German Iron and Steel Industrialists (VDESI) and the so-called *Langnam-Verein*.

industry actively advocated the introduction of a new public social policy, rather than merely consenting to an initiative of other actors (s.a. Mares 2003a: 259).

The exceptional position of work injury insurance justifies the analysis of the introduction of this policy in more detail. In order to understand the reasons for the exceptionally active role of business it is essential to look at the policy alternatives that were on the agenda and how *they* would have affected industry. The policy status quo and the policy choices promoted by other actors are the alternatives that industry compared the introduction of work injury insurance to. To understand what business expected to gain from work injury insurance it is important to know what it was thereby trying to overcome or to prevent.

Industrial employers supported work injury insurance as a lesser evil to the pre-existing employers' liability legislation, which had contributed to the aggravation of class conflicts. The compensation of workers for work injuries was regulated in the *Employers' Liability Law* enacted in 1871 (RGI 1871: 207). This law made the employer personally liable for all work injuries caused due to his negligence. To gain an entitlement for compensation, workers needed to go to court. They needed to file a lawsuit against their employer. The onus of proof was in principal on the worker.⁴⁶ In practice only about 20 to 25 per cent⁴⁷ of all work injuries were compensated. The law was generally considered as insufficient for protecting workers and the majority of injured workers continued to depend on municipal poor relief (Breger 1982: 80).

Industry viewed employers' liability rules as costly and as causing an aggravation of class conflicts. Many employers had taken out private policies to insure against the costs of compensation payments. More importantly, the confrontation of employers and workers in court had contributed to an unwelcome aggravation of class antagonisms within firms and had provided the labor unions with opportunities for mobilization.⁴⁸ Employers thought that the Employers' Liability Law unjustly turned work injuries into an offence committed by the employer, while in reality most work injuries would be caused by unforeseeable events or *force majeure*, and were thus without anybody's fault (Breger 1994: 26-28). Indeed, as work

⁴⁶ With the exception of the railway sector, where the burden of proof was on the employer

⁴⁷ The chamber of commerce in Dortmund reported a compensation rate of 25 per cent, in (Francke 1881): 404. (Breger 1994) reports a compensation rate of about 20 per cent. Also (Ritter 1983): 31 estimates that about 20 per cent of all work injuries registered were compensated. (Tennstedt 1981): 175 notes that about 10 to 40 per cent of all accidents were covered, though the actual compensation rate was lower due to bankruptcies of firms.

⁴⁸ See, for instance, reports by the chambers of commerce in Osnabrück and Dortmund (Francke 1881): 401 and 404 and the protocol of the conference in Bochum, November 2nd/3rd, 1880, where German industrialists discussed a proposal for work injury insurance (Baare 1880). See also petition of the chamber of Commerce Essen to the Reichstag, April 19th, 1881, analyzed in (Breger 1982): 83.

injuries are hardly ever caused by intention, the proof of fault turned out to be very difficult in practice, as the low compensation rate shows.

Two basic options for reforming liability legislation were on the agenda: (a) the compensation of injuries by a compulsory public insurance programme, or (b) a tightening of employers' liability obligations combined with stricter regulations for worker protection. For employers, work injury insurance provided an attractive alternative to a tightening of liability legislation. The introduction of work injury insurance effectively eliminated the obligations that liability legislation imposed on employers. Moreover, shifting the responsibility for compensation from the individual employer to a public insurance programme meant that the meaning of work injuries would also change, from something akin to an offence committed by the individual employer, to a general risk, a risk that the state had to take care of (Breger 1994: 43-44). Work injury insurance allowed industry to pass on the responsibility for compensating work injuries to the public and at the same time promised to reduce class conflicts within the firm. In particular the heavy industry, where the risk of work injuries was particularly high, hoped to reduce the cost burden of compensating work injuries by shifting costs to a broader risk pool that also included other industries with a lower risk. The perceived shortcomings of employers' liability legislation were the main reason for industry to collaborate with the government to introduce a new programme of work injury insurance (Breger 1982: 83).

The policy alternative on the agenda was a policy programme of so-called 'worker protection,' which involved the tightening of employers' liability rules. This policy programme was advocated by the social democrats, the labor unions and the bourgeois social reformers, and was supported by some senior government officials. A tightening of liability rules had been debated in the parliament. Worker protection appeared thus as a politically viable alternative. The worker protection programme meant state legislation aimed at protecting workers from work-related risks. In addition to the tightening of employers' liability rules, the programme included also proposals for the prescription of preventive measures, state factory surveyors, working time regulations and special rules protecting women and young workers. Employers wanted to avoid worker protection legislation and, in particular, strengthened liability rules (Berlepsch 1994).

Neither the social democrats nor the bourgeois social reformers perceived worker protection as an alternative to social insurance. Instead, they favored a combination of both. In a parliamentary motion of February 1879, the social democrats demanded a public work injury insurance with compulsory coverage as a complement to a strengthened Employers'

Liability Law to make sure workers would actually receive compensation (Seeber and Fesser 1994: 97-99). Still, the social democrats and the labor unions focused their demands on worker protection. The SPD had already introduced a motion for a new worker protection law in the Reichstag in April 1877. The motion included a maximum working day of 10 hours for men and 8 hours for women and young workers, a ban on work during night time and on Sundays (with exceptions), a ban on child labor, a ban for women to work underground and on construction sites, as well as dismissal protection rules (Berlepsch 1994; Seeber and Fesser 1994: 93).

At about the same time, senior state officials had also drafted a law strengthening worker protection, but Bismarck dismissed this proposal as being ruinous for industry, and shelved the draft. Worker protection and employers' liability rules would poison the relations between the two sides of industry, Bismarck believed, and would offer the unions the opportunity to play the role of workers' champions (Hennock 2007: 89). The draft law did thus not make it to the parliament for debate. Instead, Bismarck turned his attention to social insurance as a way of undermining support for the Social Democrats (Berlepsch 1994: 67). This was welcomed by the heavy industry, as it offered a way for averting the looming tightening of the 1871 Employers' Liability Law.

A crucial part of Bismarck's strategy for building up loyalty to the political regime was to pacify major social groups by offering concessions to them, expecting political support in return. Political turmoil should be forestalled at any cost. Employers' liability legislation and worker protection were intricate issues in this respect, as they required the Chancellor to make a decision that might satisfy one group, while at the same time upsetting the other. A public work injury insurance offered a way out of this dilemma for Bismarck, because it was a solution that promised to be acceptable to both sides.⁴⁹

The idea of work injury insurance was not the brainchild of Bismarck, however. The idea of establishing work injury insurance with compulsory coverage had several origins. In 1879, the opposition social democrats had demanded such a programme, as mentioned above (Seeber and Fesser 1994: 97-99). At about the same time, the chamber of commerce in

⁴⁹ In August 1879, Bismarck presented his ideas for public insurance programmes in a circular to the governments of the federal states. In addition to work injury insurance, he also proposed public schemes for life insurance, fire insurance, hailstorm insurance and cattle insurance, all on the basis of provision by state monopolies ⁴⁹ (Ritter 1983: 43). The exclusion of commercial providers from these areas of business was intended to crowd out the private insurance sector⁴⁹ (Ritter 1983: 44). The choice of risks shows that the public insurance project was initially not exclusively directed at industry and labor, but in particular also at agriculture, because Bismarck, who was an aristocratic estate owner, also wanted to consolidate the alliance with agriculture, established by the turn to protectionism in 1879.

Dortmund, a city in the heartland of Germany's heavy industry, had written to the Prussian Minister of Economics, Maybach, to demand the introduction of municipal work injury insurance programmes (Breger 1994: 25-26). Within the government, Theodor Lohmann, the senior state official in charge of social policy issues, was working on a draft for an amendment of the 1871 Employers' Liability Law that would have included legislative incentives for voluntary private insurance⁵⁰ (Hennock 2007: 99).

The heavy industry as agenda-setter

Lohmann's proposal was however rejected by Bismarck. Instead, he mandated the heavy industrialist *Louis Baare* to draft a bill for public work injury insurance. Baare was director general of a large coal and steel combine in the Ruhr ('*Bochumer Verein*') and president of the chamber of commerce in *Bochum*. Already in April that year, Baare had presented a memorandum on the work injury issue to the national Minister of Economics, Hofmann, which the latter brought to Bismarck's attention. In this memorandum Baare proposed the repeal of the 1871 Employers' Liability Law and replace it with an insurance programme. Baare proposed the establishment of compulsory insurance funds, financed with contributions from both workers and employers (Hennock 2007: 88; Breger 1994: 26).

Like other heavy industrialists, Baare was highly critical of the 1871 law because the law provided a source of ongoing confrontation and conflict between employers and workers. He expected that if industry accepted work injury insurance, this would help to get rid of the disliked liability rules: "If we are ready to make sacrifices now, we will sustain the support of the Reich government in the fight against an extension of the Employers' Liability Law" he told his fellow industrialists (Baare 1880). Baare made clear that for industry work injury insurance was the lesser evil compared to a tightened liability legislation. He reminded his fellow industrialists:

not to set the benefits of the insurance in a too narrow-minded way, as otherwise the tightening of employers' liability is definitely to be expected. If the industry is prepared to make sacrifices now, it will secure the goodwill of the government in the fight against the extension of the Employers' Liability Law (quoted from Breger 1994: 53, translated from German by TP).

Together with a small group of other representatives of the heavy industry, Baare drafted a proposal for a work injury insurance scheme. This proposal was intended as an alternative to a tightening of employers' liability legislation. To explore the extent of support for his plan within broader circles of industry, Baare organized a conference in Bochum on November 2nd/3rd, 1880. This meeting was attended by about 30 representatives, many of

⁵⁰ Employers would be freed from their liability if they provided an insurance for their workers

them from heavy industry and other “big industry” sectors. The Baare proposal received strong support at this meeting (Baare 1880; see also Bacmeister 1937: 225). Anecdotal evidence for the strong support for Baare’s proposal is also provided by the fact that after having learned about Bismarck’s decision to mandate Baare with drafting a proposal, the CDI wired a message to the Chancellor congratulating him to this decision (Breger 1994: 26).

At about the same time, senior officials in the Ministry of Economics were also working on a draft for work injury insurance (Hennock 2007: 96). The ministry draft, together with the one by the Baare group, formed the basis for the bill that Bismarck presented to the Reichstag in January 1881 (Breger 1982: 82; 1994: 27). This first bill was rejected by the Reichstag, though, and needed to be revised twice by the government before parliament accepted work injury insurance in 1884. The issues debated by the Reichstag focused on the financing and the administrative organization of work injury insurance, as well as the role of worker representatives in the administration of the programme. Once the draft moved to the parliamentary arena, the industrialists had little control over the policy-making process (Hennock 2007: 99).

Despite the subsequent changes to the bill made in the Reichstag, the contribution of heavy industry on the work injury insurance law was considerable.⁵¹ In alliance with government, heavy industry had set the course for the introduction of work injury insurance and against a tightening of employers’ liability legislation. Getting rid of employers’ liability legislation and its deteriorating effects on labor relations was the main reason why industry had supported work injury insurance (Baare 1880).

Industry’s work injury insurance proposal

The bill drafted by Baare and his collaborators contained the following elements:

- *compulsory coverage* for all workers, covering large segments of the economy, also agriculture; with opt-out possibilities for firms that are participating in occupational

⁵¹ The following paragraphs analyze the main concerns of industry regarding the design of the work injury law. The main archival sources used are the protocol of the Bochum conference (Baare 1880), an abridged version of which is reprinted in (Breger 1994: 48-60), which provides highly valuable insights into the deliberations among German industrialists; a survey of the positions on work injury insurance conducted by the Royal Prussian Statistical Office among 61 regional chambers of commerce (Francke 1881); and documents from the collection of archival sources published by the Historical Commission of the German Academy of Science mentioned above, especially (Ayass et al. 2003).

liability insurance schemes.⁵² No voluntary opting-in for groups not covered, in order to avoid an overloading with bad risks (adverse selection problems).

- *Financing* by contributions from employers (50 per cent), workers (25 per cent) and municipal subsidies (25 per cent). It was argued that the municipalities would benefit from work injury insurance because of a reduction of the burden on municipal poor relief, and they were therefore called upon to subsidize the insurance. Workers should also contribute to make sure they had a stake in the efficient administration of the scheme, so the official justification (Breger 1994: 29-30). Financing should take place on a pay-as-you-go basis, which involves less start-up costs as compared to pre-funding.
- *Administration* by an Imperial Insurance Board ('Reichsversicherungsamt') with the participation of employer and worker representatives. A centralized nationwide organization by the state was considered as cheaper and more effective than a decentralized organization through private insurance firms or liability insurance associations (see also resolution by the CDI general assembly, 1882, September 18th, Document No.33 in Ayass et al. 2003: 125; see also Breger 1994: 31).
- *Benefits* should be as low as possible and be subject to ceilings. Where feasible, the proposal preferred discretionary clauses instead of definite benefit entitlements. The first four weeks should be covered by the health insurance funds. Only from the 5th week on would benefits be covered by the work injury insurance scheme. This shifted a significant part of the costs to the health insurance funds, which were in general financed to two thirds by the worker and one-third by the employer. This was motivated by the intention to reduce the cost burden on work injury insurance, but was also defended on the grounds that the health insurance funds would be better suited to identify benefit abuse.
- Public insurance should remain limited to the risk of work injury. *No* introduction of compulsory old-age or disability *pension programmes*. This would be too expensive and promote malingering and benefit abuse (Baare 1880).

A law was passed by parliament on June 27th, 1884, which established a public work injury insurance programme with compulsory coverage. The programme was to be

⁵² In the coal industry self-organized insurance associations existed already for a long time in the form of the Knappschaften. The Knappschaften were employer-sponsored occupational insurance associations for coal miners, providing compensation for sickness and disability, (Parnell 1994: 15-19). They have served as a precedent for the so-called Berufsgenossenschaften [occupational insurance associations].

administrated by occupational liability insurance associations, the so-called *Berufsgenossenschaften*. These insurance associations had to be set up collectively by the employers on a sectoral basis. They had to collect contribution fees from member firms and pay out benefits. The Reichstag, thus, opted for corporatist self-administration instead of direct state administration, as originally proposed by the Baare group. Moreover, the law obliged employers to finance work injury insurance alone. The law stipulated that the programme has to be financed exclusively by contributions from employers. Industry had demanded additional contributions from workers and state subsidies, instead (Breger 1982: 101-103). In return, however, the health insurance period was eventually extended to 13 weeks, instead of 4 weeks. Despite these deviations from its original proposal, industry accepted the law. Industry hoped that the new law would lead to an improvement of labor relations, promote industrial peace and help to suppress organized labor (Breger 1982: 86-87).

To summarize, leading heavy industrialists had played a significant role in the introduction of work injury insurance in Germany. Heavy industry was one of the actors that have brought the issue of work injury compensation onto the political agenda. Indeed, work injury insurance is one of the very few cases where industry had actively promoted a new social policy, instead of merely responding to the initiatives of other actors.⁵³ By putting forward their own proposal they expected to be able to prevent a tightening of liability legislation. The initiative by the heavy industrialists had contributed to the introduction of work injury insurance, but it appears unlikely that in the absence of the threat of tightened liability legislation and the aggravation of class conflicts these industrialists would have supported work injury insurance. It was not alone the high risk of work injuries in this sector that led the heavy industry to support work injury insurance, but the way pre-existing institutions had turned this risk into a source of class conflict.

The ‘*Berufsgenossenschaften*’: industry against corporatism

Heavy industry had originally been skeptical about the corporatist form of insurance organization.⁵⁴ The Baare bill had proposed administration by a centralized state agency with the participation of employer representatives. Industry considered this form to be the cheapest

⁵³ The historian E.P. Hennock has argued that the claim ‘that heavy industry was shaping the provisions of the legislation are not borne out by the ... Baare correspondence. It was certainly intended to work in the interest of industrial employers, but their wishes were far from paramount’ (Hennock 2007: 96). Hennock is right that the final bill passed by parliament deviated in important ways from the preferences of the heavy industry, as shown above, but the proposal presented by the Baare group has certainly influenced the government’s draft bill.

⁵⁴ In contrast, the chemical industry had supported the *Berufsgenossenschaften* (Breger 1982: 112).

and most effective form of administration (Bueck 1905a: 208). In the end, industry accepted that work injury insurance would be administrated by so-called *Berufsgenossenschaften*, employer-organized liability insurance associations (Breger 1994: 35; Ullmann 1979: 599-600). In September 1882, the CDI declared to accept this form of organization in order not to jeopardize the passing of the bill: ⁵⁵

The delegates [of the CDI general assembly] still consider that the work injury insurance is best implemented through an Imperial Agency ('Reichsanstalt'), as originally planned....In the interest of the success of the law they do however not object to the corporative organization. (resolution by the CDI general assembly on September 18th, 1882, Document No. 33 in Ayass et al. 2003: 125).

The initiative for a corporatist organization came from Bismarck and his advisers (Hennock 2007: 99). The replacement of the planned Imperial Insurance Board by *Berufsgenossenschaften* had helped the government to gain the support of the catholic Center Party for the bill. This party was pivotal for forming a majority in favor of the law. In principle, the Center Party supported the law, but it was opposed to centralized state administration and demanded more decentralization instead (Ritter 1983: 48-49).

More generally, Bismarck intended the corporatist *Berufsgenossenschaften* to become a model for the organization and representation of economic interests within the state (Abelshauser 1984: 292-293). They should either co-exist, or even replace, the national parliament, the Reichstag, as the legislature. The reason for this was that Bismarck considered parliamentary democracy as an unreliable source of political legitimacy and was planning to set up corporatist institutions as an alternative to representative democracy (Ritter 1983: 44). In October 1883, Lohmann, the top state official in charge of social policy, reported about a meeting with Bismarck:

The work injury insurance is secondary for him. Of primary importance for him is through this opportunity to achieve corporate associations, which, in the course of time, have to be created for all productive social classes, so that one attains the foundations for a future popular representation, which will become an important co-determining factor in legislation, either instead of, or in addition to the *Reichstag*, even, if the worst comes to the worst, through a *coup d'état*. (Bismarck to Lohmann on October 5th, 1883, according to Lohmann's recollection, quoted in Ritter 1983: 44) .

Industry's opposition to worker committees

The main point of controversy surrounding the organization of work injury insurance concerned the issue of 'worker committees' ("*Arbeiterausschüsse*"). Industry could successfully prevent the formation of worker committees (Breger 1982: 117-123; 1994: 36-

⁵⁵ This analysis does therefore not confirm the finding by Mares that large industrial firms have preferred corporatist administration to state administration (Mares 2003a: 83-84).

37; Ullmann 1979: 600). The arguments used by industry in this controversy provide us with important insights regarding the attitude of industry towards the participation of labor in social policy governance. The worker committees were included neither in the Baare bill nor in the first government bill. They were introduced only by the second government bill. Each *Berufsgenossenschaft* should have its own worker committee to represent the interests of the workers (Breger 1994: 36). Due to the opposition from industry they were again eliminated from the final bill (Breger 1982: 117-120). The position of industry was, in short, the following: The participation of worker representatives in the joint administrative committees was accepted, but independent worker committees were rejected (Bueck 1905a: 258).

This position was motivated by fears about an intensification of class conflicts and a strengthening of the socialist labor movement through worker committees. The participation of worker representatives in the administrative committees was seen as necessary to ensure the collaboration of the workers. Giving workers a role in administration was thought to be essential to avoid benefit abuse and to ensure a prudent and efficient use of the insurance funds (see, for instance, the report by the chamber of commerce in Osnabrück in: Francke 1881: 401; resolution by the CDI general assembly, 1882 September 18th, document no.33 in Ayass et al. 2003: 125-126; see also Breger 1994: 36). In contrast, separate worker committees were suspected of becoming hotbeds for social democratic agitation and mobilization and of undermining the authority of the employer (Bueck 1905a: 268-269; Breger 1994: 36; Vogel 1951: 42-43). As a result, class antagonisms would intensify, instead of diminishing (Bueck 1905a: 267-268). In the larger administrative committees, in contrast, the employer side would have a majority of votes and the worker representatives could be integrated more effectively. The goals of diminishing class conflict and suppressing the socialist labor movement are thus also reflected in the disputes over the organization of social insurance.

3.III Employers' Positions on Health and Pension Insurance

Bismarck continued his strategy of pacifying the working class with plans for health insurance and disability and old-age pensions. Industry was more reluctant to support these two programmes, compared to work injury insurance, but nevertheless decided to go along with Bismarck's plans. The general motivations for support however had been similar. Industry endorsed health and pension insurance as a sacrifice necessary to pacify the working class and suppress social democracy, rather than because it thought that these programmes would be in its economic interest.

Public health insurance: crowding out union funds

Like work injury insurance, the introduction of *health insurance* was a rather uncontroversial issue and was in principle supported by industry. On June 15th, 1883 the national parliament passed a law introducing public health insurance for all workers. Workers had to pay two thirds of the contributions, employers had to pay the remaining third (Breger 1982: 54-56). Industry supported compulsory coverage for all workers as necessary to avoid adverse selection problems (Bueck 1905a: 195). Also the co-financing by employers was accepted by industry. Industry pushed for benefit levels to be low, not only to keep the cost burden low, but also to avoid malingering (Breger 1982: 61).

The main issue of conflict concerned the integration of the union-sponsored 'assistance funds' ('*freie Hilfskassen*') into the system of public health insurance. These funds were part of the highly fragmented system of health insurance provisions that had emerged in Germany since the 1850s. Company health insurance funds co-existed with municipal, guild, parish and union-run assistance funds, as well as the so-called *Knappschaften*, the occupational insurance funds for miners. Some of these insurance funds were based on voluntary, others on compulsory coverage. Some were local, others regional and others again nationwide. A law passed in 1876 ('*Hilfsgesetz*') attempted to harmonize the existing system by regulating the benefit levels and contribution rates of the union-sponsored *Hilfskassen* (Breger 1982: 54). This attempt failed because many *Hilfskassen* decided not to register for certification according to the new law and preferred to operate as so-called 'wild funds' instead, in order to avoid state regulation (Ullmann 1979: 578-579). The 1883 law maintained the fragmented organization of health insurance by mandating the existing insurance funds with administering public health insurance (Ullmann 1979: 581). In short, the 1883 law harmonized coverage, financing and benefit rules, but kept the organizational basis of health insurance unchanged.

The unions used their *Hilfskassen* as a vehicle for mobilization. The *Hilfskassen* were able to offer comparatively generous benefits by declining to accept older workers and were very popular among workers. Employers did not contribute to the financing of these funds and had no say in their administration. Ideologically, the *Hilfskassen* were motivated by the idea of 'worker independence', i.e., the idea that, as long as a socialist state was out of reach, the working class should take charge of its needs itself, without any state interference, in order to avoid any dependence on the bourgeois state. After the passing of the anti-socialist legislation in 1878, which banned the Social Democratic Party from any form of political

agitation, the *Hilfskassen* became an increasingly important organizational vehicle for the socialist labor movement (Seeber and Fesser 1994: 101-105).

Industry strongly opposed the *Hilfskassen* because it saw them as a 'hotbed for social democratic agitation and organization' (Bueck 1905a: 474). With the plan to introduce a system of public health insurance the question arose whether the *Hilfskassen* would be integrated into the new public system; that is, whether workers insured by the *Hilfskassen* would fulfill the criteria of compulsory coverage. Industry opposed this. Industry wanted that workers insured by one of the *Hilfskassen* would still be obliged to join a company health insurance fund (Bueck 1905a: 197-201). Industry did however not prevail on this point as the government gave in to demands to integrate the *Hilfskassen* (Breger 1982: 71).

The fact that industry had opposed the *Hilfskassen* indicates that the pacifying aspect of social insurance mattered much more to industry than the cost aspect. Employers opposed the *Hilfskassen*, despite the fact that they did not need to pay any contributions to them, like they had to do for the other types of insurance funds. Some organizations even called upon their members not to take advantage of cost savings by insuring their workers with the *Hilfskassen* (Breger 1982: 72). For employers, the cost advantages did not outweigh the political disadvantages of the union-run insurance funds. They were willing to accept a rise in labor costs in order to undermine the labor union movement.

The *Hilfskassen* provided the Social Democrats with an organizational vehicle for agitation and mobilization and thus threatened to contribute to the strengthening of their influence within the working class. The aim of the social insurance reforms was however the exact opposite: to fight the social democrats by pacifying the working class. The opposition of industry to the *Hilfskassen* reveals what motivated industry to support social insurance. The working class should receive social protection, but not political influence. The goal of industry and government was to suppress social democracy by pacifying the working class and thereby neutralizing the class antagonism that fuelled the growth of the social democrats and organized labor. The *Hilfskassen* were an obstacle to this goal and therefore industry wanted to crowd them out.

Disability and old-age pensions insurance

Pension insurance for disability and old age was the last of the three social insurance schemes introduced during the 1880s. The conservative heavy industrialist *Stumm* had proposed a mandatory public pension insurance already in 1878, but at that time failed to gain

Bismarck's support (Vogel 1951: 38-39). Three years later, the Imperial Message declared the government's intention to establish a public pension system (see above). In November 1887, the government presented an outline for the planned pension system. One year later, in November 1888, the government presented a bill for a disability and old-age pension law to the parliament. In May 1889, the law was passed by the national parliament (Hennock 2007: 184-187). This law introduced pension insurance benefits for disabled persons and persons above the age of 70. The scheme was pre-funded and financed by contributions from employers and workers in equal shares, plus state subsidies. Regional insurance agencies were in charge of administrating the scheme (Hennock 2007: 187-197).

Industry generally reacted with hesitation to the government's plans for public pension insurance. The CDI and other leading industry associations declared 'not to oppose' and to 'sympathize' with the introduction of a public pension system, but at the same time thought that the timing for its introduction would be premature, given that industry had just accepted to shoulder the costs of work injury and health insurance (Breger 1982: 133-134; Bueck 1905a: 324). According to industry, the introduction of pension insurance should be 'put off as long as feasible' (Langnam-Verein in 1889, quoted in Breger 1982: 133). Despite this reluctance to support pension insurance, the CDI declared itself 'ready to cooperate with the government in order to create a law that is in line with ...the requirements of the real life' (Bueck 1905a: 324). Despite the existence of some reservations, industry thus decided to cooperate with government in order to secure some influence over the outcome.

The reluctance of industry to support disability and old-age insurance was due to several reasons. First, the perception had arisen within industry that the construction of social insurance was progressing too fast and would result in prohibitive levels of labor costs. Second, industry suspected that public pensions would undermine work incentives and encourage work shirking. Disability pensions would be prone to abuse by workers because the fact of work disability would be difficult to check (Breger 1982: 133ff). According to Henry Axel Bueck, the leading spokesperson of the heavy industry, the provision of a generous public pension would cause many capable workers to leave the labor market and thereby reduce the labor supply: 'My experience is that...if a worker, under the pretence of physical disability, declares not to be able to work, nothing on earth can prove that he would still be able to do so'. Furthermore, Bueck elaborated that

If the state would promise every worker from the outset a pension for disability and old age as a legal entitlement, this would diminish the sense of individual self-reliance, and this would be the greatest damage that we could do to our society...I have said...*"to be poor must never stop being a misfortune"* This may sound very harsh, very heartless, but simply remove the perspective that presents misery, deprivation and poverty as a consequence of carelessness,

indolence, idleness and dissoluteness, and at the same moment a large share of the poor will stop to make an effort, which today, with all their energy and most of them with success, endeavor to avert this sad fate (annual report by Henry Axel Bueck to the 11th general assembly of the Langnam-Verein, 1881, November 29th, document no. 23 in Ayass et al. 2003: 97, translated from German by TP)

Third, industry had also gained the impression that its strategy of influencing social policies by cooperating with government did not show the expected results. Already in the parliamentary debates over the 1883 health insurance law, the CDI had realized that many of industry's concerns had been ignored, such as its opposition to union-run insurance funds (speech by Bueck at the CDI general assembly in Stuttgart on September 15th, 1883, see Bueck 1905a: 239-240). Moreover, Bueck indicated that the efforts to pacify the working class through social benefits may be a case of forlorn hope. There was no evidence that the social reforms so far would have weakened social democracy. In the future, industry would need to be more cautious in supporting the government's social policy plans (Bueck 1905a: 240-241). The strategy of influence by cooperation was not as successful as industry had expected. Despite these objections, industry did continue to endorse Bismarck's goal of pacifying the working class. Industry could not deny that a public pension system was in principle an appropriate tool to achieve this goal and thus eventually decided also to accept pension insurance.

In the policy-making process industry focused its efforts on two goals: to keep pension benefits as low as possible and to influence the administrative organization of pension insurance. The government had planned to mandate the corporatist *Berufsgenossenschaften* with the administration of pension insurance. The CDI had consented to this form of organization in the case of work injury insurance, but had in the meantime become more hostile to the *Berufsgenossenschaften* (Bueck 1905a: 432). The reason for this change was that the *Berufsgenossenschaften* had in the meantime developed into an organizational rival to the CDI. Up to the 1880s, the CDI had been the unchallenged political voice of German industry, despite the fact that it was far from representative of the overall economy and was dominated by the heavy industry. This threatened to change in 1887, when the *Berufsgenossenschaften* decided to form their own national federation with the ambition of developing from mere insurance associations into a political interest group for business (Ullmann 1979: 605-607; Breger 1994: 46; Hennock 2007: 189).

Being based on compulsory membership, the *Berufsgenossenschaften* were much more representative of German business as a whole compared to the CDI, which relied on voluntary membership. The *Berufsgenossenschaften* thus had the potential of becoming an

organizational competitor to the CDI as the dominant political interest group of German business. The resistance of the CDI was decisive in making the government abandon its plans to extend the Berufsgenossenschaften to old-age and disability pensions. The result was a state-based organization, relying on regional insurance agencies, instead of corporatist insurance associations (Hennock 2007: 189). In short, by cooperating with the government, industry did manage to prevent a corporatist organization of pension insurance.

3.IV Intra-Business Differences on Social Insurance

The active role played by prominent heavy industrialists in the introduction of work injury insurance and the endorsement of the social insurance reforms by the CDI and other leading industry associations suggests that German employers had predominantly supported the introduction of social insurance. CDI executive director Bueck claimed in retrospect that German industry had belonged to the ‘most effective promoters’ of the introduction of social insurance (Bueck 1905a: 792). Some scholars have argued that German industry had been internally split on the issue of social insurance. The German historian Hans-Peter Ullmann argues that large groups among German employers had been opposed to the introduction of social insurance. According to Ullmann, a small but politically powerful group of employers, the big industrialists organized in the CDI, supported social insurance, but other groups of employers had opposed social insurance. These dissenting groups were less well organized and therefore lacked the clout to shape the reform outcome. According to Ullmann, opposition to social insurance came *inter alia* from exporting manufacturing firms and employers with a politically liberal orientation (1979: in particular 592-594; see also Vogel 1951: 43-44)

Also Isabella Mares argues that employers had been internally split regarding the introduction of work injury insurance. According to Mares, work injury insurance ‘was the desirable outcome for large, manufacturing employers and primarily for producers in industries characterized by a high incidence of workplace accidents. Not all employers, however, supported these radical reforms’ (Mares 2003a: 76). In contrast, Monika Breger⁵⁶ finds that German employers supported the social insurance reforms at large: ‘The conclusion of this study, that industrial employers had supported the social legislation, does indeed hold for them as a whole’ (Breger 1982: 223, translated by TP). In a similar way, also Büren⁵⁷ found that the vast majority of German industrialists had supported the introduction of social

⁵⁶ Monika Breger is a German historian, who wrote her PhD thesis about the positions of industrial employers in Germany regarding the state’s social policy reforms between 1878 – 1891 (Breger 1982).

⁵⁷ Herbert Büren wrote a PhD thesis on the attitude of German employers towards social policy issues.

insurance (Büren 1934: 54). This divergence in findings suggests that a closer look at the extent of support for Bismarck's social reforms among German industrialists is needed. To what extent did the support for social insurance articulated by the CDI and leading associations of the heavy industry represent the positions of German business at large? Did German business stand united behind Bismarck's goal of pacifying the working class?

The most comprehensive source concerning intra-business differences on positions regarding social insurance issues available⁵⁸ is a survey conducted by the Royal Prussian Statistical Office among 61 regional chambers of commerce concerning their attitude towards work injury insurance (Francke 1881). This survey allows a basic quantification of business support for social insurance, even though the survey is limited to the programme of work injury insurance. The results of the survey⁵⁹ show that slightly more than one half of the chambers supported work injury insurance. About one fourth of the chambers would have preferred a reform of liability legislation instead of work injury insurance (see table 3.3 below). The results also show that the support was motivated by the goal of overcoming the Employers' Liability Law.⁶⁰

Table 3.3 Business Positions on Work Injury Insurance

Position taken	Percentage
Chambers considering the 1881 draft for a <i>Work Injury Insurance Law</i> to be in general a substantial improvement compared to the 1871 <i>Employers' Liability Law</i>	53 %
Chambers not considering the 1881 draft for a <i>Work Injury Insurance Law</i> to constitute a substantial improvement compared to the 1871 <i>Employers' Liability Law</i>	39 %
Chambers preferring a reform and extension of the <i>Employers' Liability Law</i> to a legal regulation of work injury insurance	26 %
Chambers in favor of private work injury insurance associations (either instead of or in addition to a state agency)	34%

⁵⁸ Unfortunately a quantification of the positions of employers regarding the other programmes is not possible within this thesis. Moreover, none of the scholars referred to above has carried out such a quantification.

⁵⁹ This is a source that is also used by Mares (2003a: 71 and 76), as well as by Ullmann (Ullmann 1979: Fn43).

⁶⁰ It should be noted that not all chambers took a position on this issue. 53 chambers did not take a position and are not included in this survey Francke 1881: 397

Chambers rejecting state subsidies to work injury insurance and, at the same time, advocating worker contributions to it.	38 %
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Source: Francke 1881: 397-398

The survey shows that business was indeed split about the advantages of work injury insurance. Far from all chambers endorsed Baare's draft for work injury insurance. A small majority of the chambers had supported compulsory work injury insurance. Support for work injury insurance went far beyond high risk sectors, such as the heavy industry, though⁶¹. Ullmann estimates that during the 1880s the CDI represented about 2 per cent of all German firms, employing about one third of all workers.⁶² (1979: 594 and Fn.47). These firms were primarily in the heavy industry and in textiles. While the CDI represented the interests of big industry, the chambers tended to represent the interests of smaller and medium-sized firms. As the chambers relied on compulsory membership for all firms in a region, their positions were more representative of the views of the business community at large than the positions of the CDI. The fact that also a majority of the chambers supported the plans for work injury insurance indicates that support for social insurance had not been limited to the high-risk heavy industry, but instead included also large segments of the rest of industry.⁶³

Intra-business differences about social insurance remained latent and did not lead to the formation of sectoral cross-class alliances. The absence of such alliances is also to be expected given that the differences did not concern so much the introduction of social insurance as such, but concerned largely details of the planned social insurance legislation, such as the financing and the administrative organization of the planned insurance institutions (Breger 1982: 227-238). These differences were thus secondary in importance and did not affect industry's general agreement with the government's plans to pacify the working class. Industry's support for social insurance was voiced primarily by the CDI, the peak-level

⁶¹ The sectors with the highest incidence of deadly work accidents were railways (597 deadly accidents per 100,000 workers), mining (261) and steel production (160) Heavy industry, together with railways, were thus the sectors with the highest risk incidence. However, support for work injury insurance came also from sectors with a very low risk incidence, such as the textiles and cotton industry, a sector that was also organized within the CDI. In textiles/leather the risk incidence was 18 deadly accidents per 100,000 workers (data on risk incidence taken from Mares 2003a: 72).

⁶² see also (Bueck 1905a: Vol.2, 259f,) who claims that the CDI represented firms employing about two thirds of all German workers

⁶³ In order to know whether positions towards work injury insurance were actually shaped by firm size and/or risk incidence it would be necessary to correlate the positions of the individual chambers with the structure of the economy in their region. Unfortunately the survey by the Royal Prussian Statistical Office does not include any data about the structure of the German economy at that time. To conduct such an analysis, these data would need to be collected separately. To carry out such a systematic comparison of the various chamber positions is therefore not possible in this chapter, neither is it available in the existing literature. Despite this desideratum, we can definitely say that a substantial part of German business did in principle support the introduction of work injury insurance.

federation of industrial employers. Despite its lack of representativeness, the CDI acted in effect as the unrivalled political voice of German industry during that time.⁶⁴ The CDI had the ear of the government and managed to influence social legislation in important respects. Differences between the CDI and smaller associations remained latent because the shared goal of crushing the socialist labor movement led the different segments of industry to sideline internal differences regarding details of policy design.

3.V Why did German Industry Support Social Insurance?

Containing the rising labor movement was the main reason that motivated German employers to support Bismarck's social insurance plans. Industry backed a strategy of labor pacification developed by the government, because it perceived its interests to be closely tied to the existing political regime. Industry perceived the capitalist order and the protection of its master-in-my-own-house attitude to labor relations to be closely tied to the consolidation of the authoritarian political regime of Bismarck. The social democrats were aiming at the political rule of the working class and the overthrow of capitalism. Industry perceived social insurance as a sacrifice that was necessary and appropriate to defeat this challenge: 'The best way for weakening the power of the social democrats is to fulfil that part of their demands that every philanthropist has to accept as legitimate' (Oechelhaeuser 1889: 109) (s.a. decision by the CDI general assembly in Dresden, September 26th, 1881, document no.33, Fn4. in Ayass et al. 2003: 125). Industry realised that it could only achieve this aim:

if the manifest grievances are corrected, which provide the social democrats with opportunities to persuade also the quiet elements of the worker population of the abjection of the existing and thereby to win them over for their revolutionary plans (Fritz Kalle, chemical industry association and Mittelrheinischer Fabrikantenverein, 1883, quoted in Breger 1982: 87).

The heavy industry spearheaded business support for the introduction of social insurance (Breger 1982: 15). This is noteworthy as heavy industry was the sector most hostile to organized labor, as we have seen in chapter 2. It refused to recognize labor unions and any form of bargaining (see Chapter 2) and was politically conservative, forming, together with the landed aristocracy, the backbone of support for the authoritarian political regime. Heavy industry was, however, not adverse to state interventions as long as they served its interest. Indeed, it had been the driving force behind the turn to protectionism in 1879. In contrast, the manufacturing industries had been politically more liberal and in favor of free trade (Kaelble

⁶⁴ Supporting the finding by Ullmann, also Hennock stresses the lack of representativeness of the CDI: 'Exactly because it was a voluntary association, the CDI was far from representative of German industry. It represented a minority able to exercise the influence of wealth and power. But it came to be regarded in government circles as *the* representative of wealth and power.' (Hennock 2007: 190, italics in original).

1967: 109-111). The manufacturing industries also abandoned their opposition to labor unions much earlier than did heavy industry, as we have seen in chapter 2. By and large, the support of the manufacturing industries for the introduction of social insurance was more low-profile compared to that of the heavy industry (Breger 1982: 223-238). This apparent paradox between anti-unionism and pro-welfarism is solved once we recognize that industry supported social insurance as a weapon for defending the traditional authorities within firms as well as within the state.

The importance of the social democratic challenge for compelling industrial employers to endorse the introduction of social insurance becomes even clearer when we conduct the following counterfactual thought experiment: Would employers have supported the introduction of public social insurance also in the absence of a politically radical social democracy? We can answer this question in the affirmative only if we can find plausible theoretical reasons for arguing that employers have an economic self-interest in public social insurance, an interest independent of the existence of the socialist challenge. In the absence of a radical socialist labor movement, a hypothetical business initiative for social insurance would need to rely entirely on economic interests in social insurance.

Such an economic self-interest may be theoretically derived from the dependence of firms on a cooperative and skilled workforce. The provision of social protection may, for instance, help firms to improve worker loyalty and work motivation or encourage them to invest in skills. To satisfy these objective interests, employers are however not bound to rely on the state. They can in principle also try to achieve these goals through other means, in particular by providing occupational social benefits on their own. This is also what many large German firms had already been doing in the late 19th century. Already before the introduction of social insurance in the 1880s, many large firms had developed their own company welfare programmes, among them the industrialists Borsig, Krupp, Siemens and Stumm (Vogel 1951: 35; re. Siemens see also Burhenne 1932). These programmes were influenced by pre-industrial, feudal ideas of patriarchal welfare. They were motivated by a combination of sense of social responsibility and employer interests in a loyal and productive workforce (Breger 1982: 245-247; Vogel 1951: 36-37). As noted by Kocka, big industry firms had developed:

indirect techniques of integration and discipline which had enabled [them] to avoid direct confrontations with labor. Through company pension funds, bonuses, works' magazines, anniversary celebrations, lectures and other welfare benefits, employers had tried to generate employee loyalty and dependence and in this way reduce the opportunities for trade union influence (Kocka 1984: 71).

Employers also provided these occupational social benefits also because they were expected to tie workers to the firm. Firm-sponsored occupational benefits were expected to strengthen workers' loyalty to their employer by evoking among workers a sense of gratitude to their employer. Workers would come to see their employer as a benevolent person and thus become more inclined to abandon their socialist loyalties. Industrialists considered as important "to keep awake the worker's feeling of dependence (*'Anhänglichkeit'*) on his employer; to get across to the worker that there is a certain identity of interests, that the employer does not stop to consider the care for the worker as being his obligation" (CDI representative Jencke in March 1889, quoted in Breger 1982: 137). Industry thus understood occupational social benefits as an important instrument for creating worker loyalty and for undermining the support for the socialist labor movement among their own workforce.

Firm-sponsored occupational social benefits are an alternative form of social pacification. The potential of firm-sponsored benefits to create worker loyalty is however undermined by public social policies, because the latter reduces the workers' dependence on benefits from the employer. Many employers in the 1880s have been well aware of this. They accepted that public social insurance was necessary to pacify the working class, but were at the same time concerned that this would weaken the dependence of the individual worker on his employer. Public social insurance would make workers grateful to the state, and not to the employer (annual reports by the chambers of commerce in Osnabrück and Essen, cited in Breger 1994: 42; 1982: 136-139; Ullmann 1979: 587). From the employer's point of view, the character of public social insurance was thus, in other words, dialectic. Fears about the crowding out of company pension schemes also contribute to an explanation of the reluctance of industry to endorse pension insurance (Breger 1982: 136-137; Ullmann 1979: 586; Vogel 1951: 45). In short, the formation of the welfare state undermined employers' ability to tie their workforce to their firm by crowding out firm-sponsored occupational benefits. Why did industry allow this to happen?

The presence of the social democratic challenge, however, compelled industry to accept a transfer of social protection from the firm to the state. Industry perceived the survival of capitalist entrepreneurship to be closely tied to the survival of the authoritarian political regime. In their orthodox Marxist orientation the social democrats constituted a fundamental challenge to the industrialists. To ward off this challenge industry needed to accept that in the future the state would be likely to reap the rewards of worker loyalty, rather than industry itself. In the absence of a radical socialist labor movement firm-sponsored occupational social

benefits would have provided a superior way for industry to create worker loyalty and motivation. To conclude this counterfactual argument, in the absence of the social democratic challenge, German industry would very likely have preferred to serve its need for a loyal and productive workforce with occupational welfare. It would therefore have been unlikely to support state institutions of social protection, which tends to crowd out occupational welfare. The challenge posed by the socialist labor movement however compelled industry to accept the transfer of social protection provisions to the state as a lesser evil.

Conclusions

Bismarck's social insurance reforms provide a clear case of *politics of pacification*. While today social insurance is often understood as an accomplishment of the labor movement, German social reformers at that time intended social insurance as a weapon against the labor movement. Social reformers intended the social insurance reforms as a tool for the pacification of the working class and the stabilisation of the existing political-economic order. The introduction of social insurance was the product of a political alliance between the authoritarian government of Bismarck and powerful groups of industrialists. Both actors understood social insurance as a tool to contain the growth of the labor movement. The working class was offered social protection in order to prevent it from claiming political power.

Industrialists supported the formation of the Bismarckian welfare state in order to pacify the working class and contain the rise of social democracy, and not because they wanted to design a policy framework conducive to labor productivity and economic efficiency. Political interests trumped economic interests. A genuine belief that the rise of social democracy needed to be stopped combined with strategic considerations to convince the leading industry associations to cooperate with the government in the drafting of the social insurance legislation. These industrialists supported social insurance because they expected social protection to be an effective way of pacifying and appeasing the politically discontent working class. Support for social insurance was particularly strong in the heavy industry, which was the sector most hostile to labor unions and social democracy. In addition, the heavy industry, where the risk of work injuries was high, also had a particularly strong interest in eliminating conflicts over work injuries that resulted from the existing liability legislation, which were grist to the labor unions' mills. Work injury insurance offered a convenient way for removing the notoriously contentious questions of work injury compensation from the sphere of labor relations by moving responsibility to the state instead.

In addition, strategic considerations also played an important role. By offering its cooperation and support, industry expected to be able to influence important details of the proposed legislation and sustain the goodwill of Bismarck towards industry's interests. Moreover, the introduction of protectionist tariffs in 1879 had eased competitive pressures on German industry, reducing the salience of the labor cost issue. In the policy-making process, the focus of industry was on keeping benefit levels as low as possible, forestalling opportunities for benefit abuse and restricting the institutional opportunities for mobilization by organized labor (Breger 1994: 43-47). In short, industry's support for social insurance was motivated by a combination of genuine preferences (pacification) and strategic considerations (influence).

The expectations of industry had only partly been fulfilled. Neither had industry's demands been fully accepted nor had the expected reconciliation of the working class occurred. First, despite its willing cooperation with the government, not all of industry's demands were implemented, as CDI executive director Bueck had complained (Bueck 1905a: 432-3). Industry managed to limit the influence of worker representatives in insurance administration by preventing independent worker committees (*Arbeiterausschüsse*), but did not manage to prevent the integration of the union-run health insurance funds (*freie Hilfskassen*) into public health insurance. More importantly, 'the goal to conciliate the masses has not been achieved' as Bueck pointed out with disappointment (Bueck 1905a: 792). Electoral support for the social democrats soared after the abolition of the anti-socialist legislation in 1890 (see table 3.1 above). Consequently, from the 1890s onwards, industry became increasingly more reluctant to support government plans for the expansion of social policies (Büren 1934: 60-74).

The findings of this chapter provide important insights that help to explain the role of employers in the formation of the welfare state. The Bismarckian social reforms were the project of a conservative state elite, aimed at stabilizing the existing political order. Neither the conventional labor mobilization approach nor the cross class coalition approach explain appropriately why German employers have supported the introduction of social insurance. Following the conventional labor mobilization approach, we would expect the acceptance by German employers of social insurance to reflect an erosion of their political power. In contrast, the cross class coalition thesis argues that employers had a genuine economic self-interest in the welfare state and thus colluded with labor to promote its formation and

expansion, rather than having been forced to accept the welfare state by an overwhelmingly powerful labor movement (e.g. Swenson 2002).

Neither has really been the case. Irrespective of how we operationalize it, there appears to have been no objective erosion of capitalist power in the 1880s. The ‘master in my own house’ approach was the prevailing approach to labor relations among German industrialists during that time (Büren 1934: 60-74; Vogel 1951: 37-38). No collective agreements constrained the exercise of entrepreneurial freedom. The CDI enjoyed close ties to the government and was an eminently powerful organization, able to influence government policy in many fields. At the same time, the anti-socialist legislation had kept the parliamentary strength of the social democrats low (see table 3.1 above). The objective strength of the labor movement, measured either as parliamentary strength or as union density, was thus still very low. There has thus arguably been no objective erosion of ‘capitalist power’.

Rather than any objective erosion in capitalist power, a *perceived danger* of an erosion of capitalist power motivated industrialist to back social policies. The granting of social protection should prevent workers from claiming political power. The rising popularity of the Social Democrats and the labor unions threatened to undermine the traditional power structures in state and economy. The authoritarian attitudes that were prevalent among German industrialists during that period excluded any form of power sharing with the organizations of the labor movement. Moreover, social democracy at that time still relied on an orthodox Marxist ideology aimed at ‘transcending Capitalism’ (Berman 2006: 35-36). Its main goal was not social reform, but to overthrow capitalist class rule and replace it with the political rule of the working class, leading to socialism. Government and industry both perceived social democracy as a revolutionary force, a force that due to its political goals could not possibly be integrated into the existing authoritarian political order and therefore needed to be defeated. The perceived radicalism of the challenge, rather than the objective political strength of the labor movement, compelled employers to support social reforms.

This chapter has shown how the historical context has affected the social policy preferences of German employers in the 1880s. Industrialists’ preference for social insurance had been genuine in the sense that they held a genuine desire to defeat social democracy and maintain the existing political-economic order. Industrialists’ support for social insurance has been a response to challenges created by the political environment and not the product of any non-ideological, objective managerial requirement for a skilled and productive workforce.

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The following chapter looks at how the enormous transformations created by World War I and the subsequent political revolution led employers to fundamentally re-evaluate their relations the socialist labor movement and to actively seek cross-class collaboration.

4 World War I and its Consequences: Class Collaboration in Exceptional Times

World War I and its domestic repercussions produced a critical juncture in the development of the German political economy. At the end of World War I, German industrialists signed an agreement with organized labor, which fundamentally reorganized industrial relations, known as the Stinnes-Legien agreement. With this agreement, German employers accepted, among other things, the recognition of unions, sectoral collective bargaining, works councils and the eight hour working day. Before the war, German industrialists had, with few exceptions, opposed negotiating with organized labor, after the war they had been actively seeking collaboration with organized labor and made major concessions to secure union collaboration. What made such a fundamental shift in employer attitude towards organized labor in such a short period of time possible?

World War I had changed the role of the state vis-à-vis industry. To simplify, before the war, capital had the state as its ally; after the war it faced the state as a potential enemy. Two distinct changes occurred during this short period that together transformed the structure of class power: First, the changing relationships between state, capital and labor as a result of the reorganization of the economy during the war, and second, the uncertainty over the future role of the state created by the revolutionary situation that followed Germany's defeat in the war. This chapter analyzes, in turn, the relevance of these two changes for the radical re-orientation of German employers' politics toward organized labor. First, the chapter looks at how the reorganization of the economy for the war effort had changed the power relations between capital and labor. Thereafter, the chapter considers the relevance of the revolutionary situation that followed Germany's defeat in the war. Finally, the chapter examines the Stinnes-Legien agreement, the first major attempt of class collaboration in German history, and what motivated employers to seek class collaboration, as well as the subsequent erosion of this compromise.⁶⁵

⁶⁵ The sections about World War I draws in particular on the study of the effects of the war on class relations and class conflicts in Germany by Jürgen Kocka, one of the foremost economic historians in Germany, which was first published in German in 1973 (Kocka 1973) . When citing from this work in the text, I refer to the English translation of the book, published in 1984 under the title "Facing Total War, German Society 1914 –1918 (Kocka

4.I Class Relations during the War: The State Changes Sides

The war had led to a fundamental change in power relations between capital and labor. Up to World War I, capital had the German state as an ally against organized labor: the war changed that. Like in the other war-waging nations, the economic and technological effort needed to wage the war⁶⁶ strained the economic resources and administrative capacities of the German state. In response to this, the governments of Germany and the other major combatant nations all expanded their control over the economy. New ministries and state authorities were established to organize the war effort and tax levels were increased substantially. As imports and raw materials were generally scarce and the labor supply constrained by the war's demand for soldiers, all economic production needed to be directed as far as was possible towards strategically important industries.

The state-led reorganization of the German economy for the war effort meant that market competition ceased to be the prime mechanism for the distribution of economic resources and was replaced by state economic planning instead (Feldman 1992 [1966]: Ch. I-V). Prices for essential goods, including cloths and foodstuff, were either decreed by the state or the goods were distributed by issuing ration cards (Carr 1979: 231-232). The allocation of raw materials and of workers, both scarce resources, was controlled by state authorities, such as the War Raw Materials Department (KRA, *Kriegsrohstoffabteilung*) located at the Reich Economic Office (RWA, *Reichswirtschaftsamt*) (Kocka 1984: 73; Feldman 1976: 316). All this amounted to a radical departure from the state's pre-war economic liberalism.⁶⁷

For German business the reorganization of the economy meant a substantial curtailment of entrepreneurial freedom. Whether a firm was making large profits, as many firms did during the war, or had to close down its factories, was now not so much dependent on its competitiveness in the market but on decisions made by state authorities (Kocka 1984:

1984), as well as well as the benchmark study by Gerald Feldman of the relations between army, industry and labor in Germany during World War I (Feldman 1992 [1966]) Furthermore, the section also draws on Leckebusch (Leckebusch 1966: in particular 60-68)

⁶⁶ World War I introduced the usage of entirely new technologies of warfare, such as the use of tanks, armoured cars, machine guns, submarines and chemical warfare. World War I is sometimes referred to as the war "waged with 20th century technology and 19th century strategies"

⁶⁷ As the historian William Carr has pointed out:

"war-time collectivism"...was a frank admission that the free working of the market economy could not be tolerated in times of economic crisis; central controls had to be imposed on the system in the interest of national survival. [Germany's] *Kriegswirtschaft* became the prototype of economic planning for twentieth-century Europe (Carr 1979: 232, italics in original).

73). In short, the war had profoundly changed the relationship between state and capital. The non-interventionist pre-war state of affairs had been shattered (Feldman 1976: 315-317).

While the war-time extension of state control over the economy, depicted as 'bureaucratic state socialism',⁶⁸ was not specific to Germany, what was specific for Germany in particular was the government's strategy to harness the collaboration of organized labor and organized employers for the organization of the war-time economy. Unions and employer associations were mandated by the government to take joint responsibility for the governance of newly established institutions for the organization of the war-time economy. The incorporation of organized labor into the governance of the war-time economy was a concession to labor that was made possible by a reversal of the state's approach to the labor movement, which business was forced to accept. Army and government were actively seeking the collaboration of organized labor in order to secure popular support for the war. The extension of government controls and the state's turn to organized labor had alienated capital from the state in a profound way and left capital without any political ally.

Organized labor as an esteemed ally of the state

At the same time as the German state extended its control over the economy to focus productivity, it was also seeking to secure the political loyalty of the working class. This need of the state to secure the political loyalty of the working class to the existing political regime, already an important motivation for social policy reforms before the war (see chapter 3), was greatly amplified by the war. The army and the state bureaucracy deemed the collaboration and support of the union leaders as essential for winning the war. During the course of the war the economic hardship and deprivation of the working class had greatly intensified and led to massive political discontent among the workers: 'Bitterness over economic misery, longing for peace, social protest and frustrated expectations of reform have been...the chief components of the discontent and bitterness which more and more came to characterize the mood of the ...masses' (Kocka 1984: 59). As all economic efforts had to be focused on the war effort, the occurrence of domestic social conflicts and strikes would have been destructive. In this situation, state and army appealed to the social democratic labor union leaders to make an effort to discipline the working class and mobilize it behind the war effort.

The rapprochement in the relations between the state and labor resulted in a novel state-labor alliance. Thereby, military and government intended to ensure themselves of the

⁶⁸N.B.: a depreciative term used in Germany by those hostile to the reorganization of the economy

loyalty and collaboration of the labor unions in the war effort, while union leaders expected to gain influence and recognition in return. While in the decade preceding the outbreak of the war, tensions between labor, business and the state had increased, the onset of the war had resulted in what was called 'sacred truce policy' (*Burgfriedenspolitik*).⁶⁹ 'Sacred truce' meant the general agreement between all major political actors, including also the social democratic party and the social democratic unions, to put on hold all domestic political conflicts as long as the war was going on. The labor movement, in effect, committed itself to abandon class struggle and its political goals more generally (socialism) for the period of the war. While in the years before the war the social democrats had been opposed to war, they reversed their position at the start of the war. The vast majority of social democratic deputies in the *Reichstag* had in 1914 voted in favor of the war loans needed by the government to finance the war. The leadership of the social democratic party had become convinced that Germany was actually under attack and had decided to support the war out of a sense of patriotic loyalty with the German state⁷⁰ (Miller 1974).

The social democratic unions, like their Christian democratic and 'yellow' colleagues, agreed to the *Burgfrieden*. Unions declared that, for the period of the war, they would abandon all strike action, not demand any wage increases⁷¹ and be willing to cooperate with employers and the state in the organization of the war economy. The support of the unions for the sacred truce and their willingness to cooperate with state and business facilitated a rapprochement between capital, labor and the state. The unions gained the political and legal acceptance by the state and, initially, also some measure of goodwill by employers, which tacitly had come to recognize union leaders as being quite pragmatic and practically minded persons.

The period of class confrontation appeared to be over. 'The dictatorship of revolutionary slogans has been broken,' wrote the *Deutsche Arbeitgeberzeitung*, one of the major employer association newspapers, 'not through the intervention of the State but through the vicissitudes of world history' (DAZ, Vol.13 August 2nd 1914, translation taken from Kocka 1984: 68). Business thought that class confrontation would subside as a result of the strengthening of feelings of national solidarity within the working class. Reflecting this view, *Emil Kirdorf*, director of the *Gelsenkirchen* mining company, declared in the spring of

⁶⁹ The famous statement by emperor Wilhelm II made in the Reichstag after the outbreak of war succinctly reflects the mood of truce "I know no political parties any more, only Germans"

⁷⁰ The decision by the social democratic leadership to support the war had later lead to a split within the social democratic movement. In 1916 leftwing factions within the party that opposed the war left the party and formed the 'Independent Social Democratic Party'.

⁷¹ Due to the shortness of labor supply, nominal wages were, nevertheless, rising substantially during the first years of the war (Erdmann 1966). Real wages, though, declined during the war due to high inflation.

1915 ‘that the patriotic spirit amongst the labor force is unquestionable...Workers called upon to join up responded to this call with enthusiasm...In such a labor force the patriotic spirit will always remain alive’ (quoted in Kocka 1984: 68).

The Patriotic Auxiliary Services Law: Concessions to Organized Labor

The labor unions new-gained role materialized in the so-called War Auxiliary Services Law (“*Hilfsdienstgesetz*” or HDG). This law was adopted by the Reichstag in December 1916 and brought legal recognition and institutional integration for organized labor. The purpose of the law was to mobilize additional resources for the war effort by introducing a new programme of compulsory civilian mobilization that covered all of the adult, male population. Since the start of the war Germany was suffering from a severe lack of skilled labor. The army and the defense industry were engaged in a fierce competition for labor resources and the lack of labor supply had put severe constraints on the defense industry to boost its production output (Feldman 1992 [1966]: 64-73).

After the intensification of the war in the summer of 1916, the army responded with the so-called ‘Hindenburg programme’. Paul von Hindenburg, the Supreme Commander, ordered a doubling of the production of munitions and the tripling of the production of machine guns. According to the defense industry, this goal would require an additional 2 to 3 million workers (Feldman 1992 [1966]: 198-199). Given the strained situation on the labor market, the implementation of the programme required either the removal of troops from the front or the mobilization of additional workers for the defense industry. To avoid the former the army eventually proposed a new programme of compulsory labor, which led to the *Auxiliary Services Law*. This law mandated that ‘[e]very male German between the ages of seventeen and sixty who is not serving in the armed forces is obligated to perform Patriotic Auxiliary Service during the war.’ (§1 of the Auxiliary Services Law of December 5th, 1916, reprinted in Feldman 1992 [1966]: 535).

Compulsory civilian service only made sense if, at the same time, the free movement of labor would be restricted. After all, what would be the point of allocating workers to munitions factories, if they would be free to change job at any time? Compulsion against labor mobility was, however, a delicate issue as the labor unions were opposed to that. Excessive labor mobility, caused by intense wage competition among firms to attract skilled labor, had already been a serious problem in some industrial districts before the introduction of the auxiliary services programme (Feldman 1992 [1966]: 74-79).

The metal industry in Berlin had approached the government with a proposal to restrict labor mobility by making the worker's right to change job dependent on the consent of his present employer. The employer had to issue a 'leaving certificate' to the leaving worker to enable him to be hired by a different employer. If the employer, for some reason, refused to issue a leaving certificate the worker was unable to change job. The government however was reluctant to use compulsion to limit labor mobility and called on industry to rely on voluntary agreements to reduce labor mobility instead (Feldman 1992 [1966]: 81). The state feared that compulsion would cause strikes and non-cooperation by the unions (Feldman 1992 [1966]: 86).

Such a voluntary agreement to control labor mobility was achieved in February 1915 between unions and employers in the Berlin metal industry (Feldman 1992 [1966]: 77). The agreement established a so-called 'War Board', a committee for the settlement of disputes over labor mobility, consisting of an equal number of union and employer representatives. If an employer refused to issue a 'leaving certificate', the worker could turn to the War Board, which would then decide about the legitimacy of the worker's request to leave and, if it considered the worker's complaint just, would issue a leaving certificate to him, which the worker could use in place of the employer's certificate (Feldman 1992 [1966]: 78). The agreement meant that the unions had to sacrifice their principle of free movement of labor but it allowed them to gain influence. The agreement gave them recognition by the employers and the settlement of conflicts on the basis of parity representation of both sides (Feldman 1992 [1966]: 78).

The War Ministry advocated the extension of the 'Berlin model' of parity-based war boards to the whole of the economy, but the proposal met with massive resistance from employers in other areas. The VDA had called on employers in other regions and sectors not to copy Berlin's war board model (Schönhoven 1987: 255). The War Ministry threatened to set up public mediation boards where the voluntary introduction of parity-based war boards failed due to employer resistance (Feldman 1992 [1966]: 88). The 'Berlin model' had found very few followers among firms from other regions and sectors. Employers generally opposed it on the grounds that these committees would establish a problematic precedent for the organization of the post-war economy. The most violent resistance came from heavy industry (Feldman 1992 [1966]: 90). Privy Councilor Hilger, a heavy industrialist from Upper Silesia, expressed the position of the industrialists clearly:

I see in these arbitration agencies an extraordinarily great danger. They will not be terminated after the end of the war. That is a belief in miracles. I am completely convinced that when we once have them we will never get rid of them, and then a breach is shot through our social

position (statement by Privy Councilor Hilger, Nov 16, 1916, quoted in Feldman 1992 [1966]: 91)

Employers explicitly linked their opposition to an extension of the Berlin War Boards to differences in union strength. Such a concession would not be necessary in other regions, where unions would be much weaker than in Berlin. In a meeting with a representative of the War Ministry in March 1916, employer representatives pointed out that the situation in Berlin would not be characteristic for the rest of Germany. In Berlin the majority of workers were unionized, in the Ruhr and in Upper Silesia, the centers of Germany's heavy industry, the unions would be much weaker (statements by Dr. Hoff, VDESI and Dr. Tänzler, VDA referred to in Feldman 1992 [1966]: 89). Class collaboration was thus explicitly rejected on the grounds that union weakness did not require it.

German employers failed to assert themselves against the labor-state alliance in favor of the war board model. As part of the Auxiliary Services Law parity-based arbitration committees were made mandatory. The law restricted labor mobility by making a change of job contingent on the employer's consent. At the same time, the law established parity-based arbitration committees to settle disputes emerging from this restriction (§ 9 of the Auxiliary Services Law of December 5th, 1916, reprinted in Feldman 1992 [1966]: 537-538}. This rule was one of several concessions made by the government to the union leaders.

The Auxiliary Services Law represented a triumph for the quest of labor union leaders for influence and recognition, a triumph that was made possible by the fact that the war effort made the union leaders valuable partners for the state. The severe food crisis in the winter of 1916/17, the so-called 'turnip winter', intensified the political discontent of the working class (Carr 1979: 236) and fuelled the anxiety within army and government about potential mass strikes. Foisting the planned programme of compulsory labor service on the workers against their will may have added further fuel to the flames of worker discontent. An agreement with labor union leaders was therefore needed to ensure their help in calming the working class. As General *Gröner*, the head of the newly established Reich War Office, which was to direct the new mobilization programme, stated: 'The task is extraordinarily difficult. It can only be solved in the closest understanding with industry and labor. The War could in any case not be won against the opposition of the workers' (quoted in Kocka 1984: 136).

Industry was in favor of the new mobilization programme but resented the concessions made to organized labor (Feldman 1992 [1966]: 195) because of their precedent-setting character, as noted by Kocka: 'During the legislative process the unions and the SPD,...,

succeeded in implementing changes in the Law which the entrepreneurs were forced to accept, although very unwillingly and on certain conditions. One of these conditions was the restriction of the law to the period of the War only' (Kocka 1984: 136).

In addition to the parity-based war arbitration committees, the introduction of mandatory '*workers' committees*' in all auxiliary service firms with more than 50 workers (§ 11 of the Law) was another major concession to labor. Despite their limited competencies, these committees signified the end of unlimited entrepreneurial authority. The worker committees established in the auxiliary service firms became the precedent for the Works Councils Law adopted after the war, in February 1920. Before, mandatory works councils only existed for large coalmines, where works councils had been made mandatory in response to a strike in 1905 (Müller-Jentsch 1986: 217; Kocka 1984: 137).

The crumbling of the 'sacred truce'

The Patriotic Auxiliary Services Law is likely to have contributed to the crumbling of the class truce, which had already set in before the passing of the Law. While the Law enforced the cooperation between business and labor, it was also instrumental in strengthening the anti-interventionist resentments among business (Kocka 1984: 140). After the outbreak of the war the relations between employers and unions had initially improved in the wake of the 'sacred truce' policy endorsed by the social democratic unions and the SPD, as shown above. Joint committees ('*Arbeitsgemeinschaften*') of unions and employers were established in sectors where cross-class cooperation had already existed before the war, dealing with social issues, such as the integration of war-disabled workers into the firms (Kocka 1984: 69; Leckebusch 1966: 62; Tänzler 1929: 109). However, this truce had already started to dissolve in late 1915, when the first wildcat strikes occurred. In the course of the war, with a quick victory becoming ever more illusionary and the material living conditions of the working class deteriorating, the class truce became more and more difficult to sustain. The political radicalization of the working class was looming, while, at the same time, business developed an increasing hostility towards state interventionism and war-time collectivism (Kocka 1984: 140).

The economic planning machinery created by the army and its attempts to tie the unions into the mechanisms of this machinery meant that business had lost its erstwhile ally: the state. In general, German business opposed the integration of the unions into the organization of the economy, and was forced to accept the newly created institutions. As noted by Kocka:

In general German industrial employers and their representative organization, the 'Vereinigung Deutscher Arbeitgeberverbände', flatly rejected the completely non-revolutionary offers of cooperation and demands for co-determination by the unions. Where a cooperative equality of the two classes prevailed in large-scale industry during the War, this usually occurred through the insistence of the unions, against the will of the entrepreneurs and under pressure from the military and civilian authorities (Kocka 1984: 69).

The loss of entrepreneurial freedom due to war-time collectivism was acceptable to industry only as a temporary sacrifice, perceived as necessary to win the war. As a rule, business opposed the new union powers institutionalized by the Patriotic Auxiliary Services Law and stressed that their validity had to be limited to the period of the war and should not be seen as a precedent for the post-war organization of the economy. Noticing the increasing indulgence by the state to the demands made by organized labor, the willingness of business to accept state interventionism went down even further.

Industry insisted on the temporary nature of the new labor-integrative institutions. In August 1917 the *Association of German Iron and Steel Industrialists* issued a petition to the national government demanding the restoration of entrepreneurial freedom by the state (Leckebusch 1966: 65). In June 1917, the VDA petitioned the National War Office ("Kriegsamt"), protesting against the allegedly hazardous effects of the Patriotic Auxiliary Services Law on firms. The VDA stressed that the concessions wrested under the pressure of the necessities of war would only have transient validity and would in no way include a commitment for the period after the War (Leckebusch 1966: 65). Also in 1917, the general assembly of 'Arbeit Nordwest', the regional employer federation for north-western Germany, where the country's heavy industry is concentrated, expressed its expectation that 'with the discontinuance of the root cause ["Entstehungsursache"] of the Law, i.e. the return to peaceful circumstances, also the institutions of the Law – the obligatory worker committees and arbitration boards – will be abolished, because during peacetime such institutions should be left to the free decision of the employer' (Braun 1927: 35-36).

In a similar way, one of the major employer associations' newspapers (*Der Arbeitgeber*) demanded in early 1918 the abolition of the new institutions for labor representation: 'They should and must fall, when the war is over, and there will be few who regret that, because every single one has felt their repressive restraints...The free entrepreneurial initiative meets with restraints and bounds wherever...entrepreneurial daringness and the energy of the genius...is replaced by...mediocrity and moderateness' (*Der Arbeitgeber*, 1918, no.1, p.2, translated by TP, quoted in Leckebusch 1966: 67-68). Heavy industry, in particular, characterized by its traditional 'master-in-my-own-house' approach,

was hostile to the integration of labor unions that was forced upon it by the War Auxiliary Services Law.⁷² In a memorandum published in the summer of 1918 the Association of Coalmines (“Zechenverband”) maintained that ‘It is almost unnatural to grant a right of codetermination in business administration, issues of wages and price decisions to the ...labor organizations or their leaders, who bear no responsibility for the prosperity of the enterprise and bear no risk’ (Osthold 1934: 259-260).

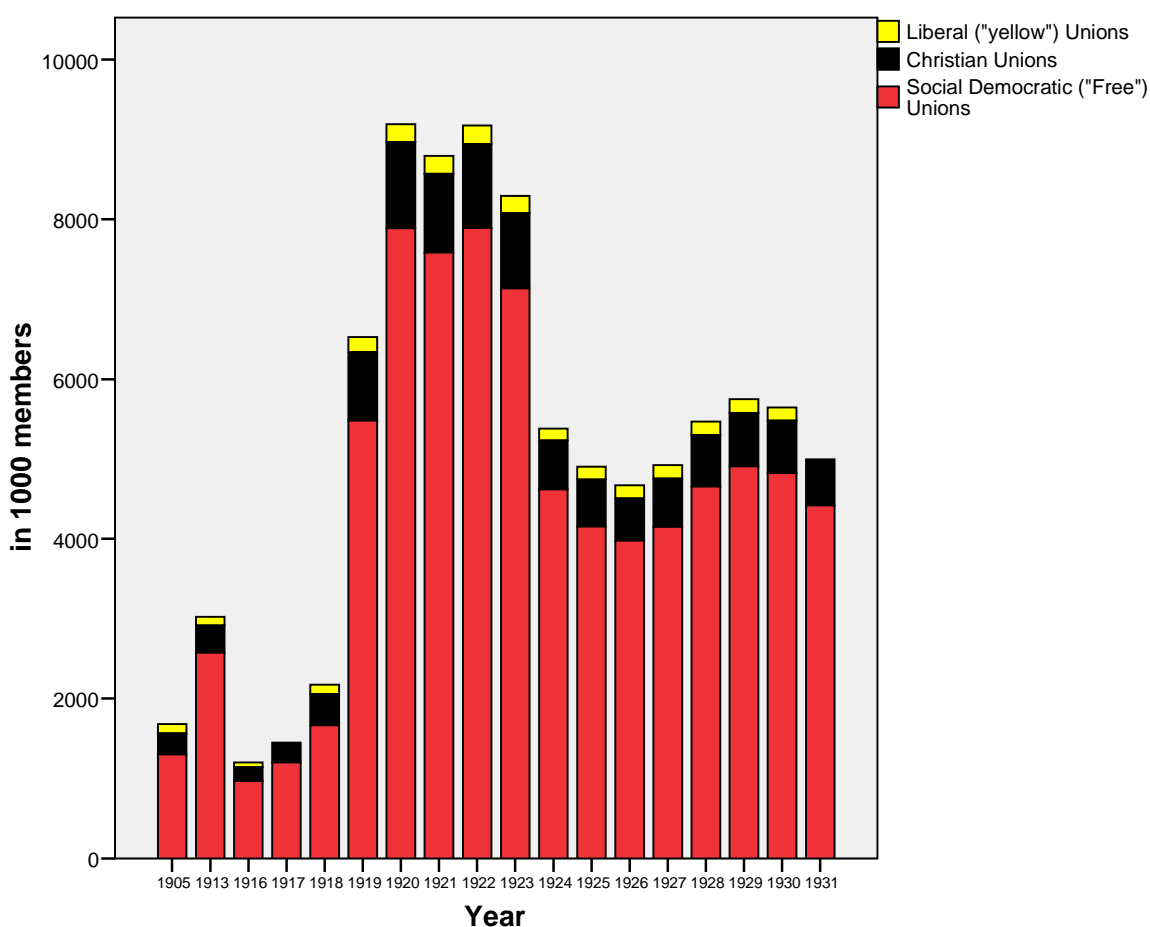
The deterioration of employer-union relations in the course of the war resulted in large part from employers’ response to the encroachment on entrepreneurial autonomy by government controls and the strengthening of the political and economic power of the labor unions. The initial period of truce gave employers reason to believe that the war would lead to a calming of the class conflict and cause revolutionary ideas to lose ground within the working class. A moderation of labor demands and labor politics did, indeed, take place in the beginning of the war, reflected in various forms of voluntary cooperation between capital and labor and an initial commitment to refrain from strike action. This initial rapprochement, though, turned out to be unsustainable and class relations deteriorated, in particular, in the years following the passing of the Patriotic Auxiliary Services Law, which enforced the cooperation of capital and labor in the organization and implementation of war-time economic planning.

As they had done also before the war, German industrialists after 1915 restarted to finance non-confrontationist ‘yellow unions’ (*wirtschaftsfriedliche Werkvereine*) on a widespread basis (Kocka 1984: 70-72). In the period of the ‘sacred truce’, employers had temporarily refrained from supporting the yellow unions. The promotion of yellow unions was intended to weaken the social democratic unions and help employers to get a foothold within the working class. This strategy of divide and conquer remained ultimately unsuccessful and yellow unions always remained very weak also throughout the war. Social democratic unions remained by far the largest ones (see chart 4.1 below). The fact that employers resorted to this anti-union strategy shows that their fundamental attitudes to the union movement had remained essentially unchanged throughout the war period, despite the initial rapprochement that resulted from the sacred truce.

⁷² In contrast, in many sectors of the peacetime industries, characterized by smaller manufacturing firms, cooperation between employers and labor tended to be more peaceful also during the war. In those sectors, where collective agreements had already been signed before the war, in particular building, wood, decoration, brewing, tailoring and printing trades, these voluntary forms of collaboration were even strengthened during the war (Kocka 1984: 69). However, this does not change the fact that, over the course of the war, attitudes among German industrial employers in general had shifted against cooperation with the labor unions.

German employers had, in essence, not changed their hostile attitude towards the social democratic labor unions, organizations to which large parts of the German industry had even refused any right to exist just a few years earlier. German industrialists, like the state elite, believed initially that the nationalist project, and the expected military victory, would lead to the permanent pacification of the working class and to the political end for the socialists. These expectations were disappointed by subsequent developments: massive discontent among workers, a strengthening of revolutionary forces and a certain estrangement between moderate union leadership and radicalized working class masses.

Chart 4.1 Labor union strength in Germany 1905-1931 (in 1000 members)



Source: Kocka 1984: 66 (for the period 1905 to 1919 and Preller 1949: 204 (for the period 1913 to 1932), in addition Erdmann 1966: 109 and Raumer 1954: 432 for 1921, Tänzler 1929: 27 for 1905 and Tänzler 1929: 117 for 1917. sources checked for consistency of data. Missing: data not available

The main impact of the war on the political positions of German employer associations was the development of a fierce opposition to state interventionism (Kocka 1984: 140). Before the war, business could rely on the state as a firm ally in the defense of entrepreneurial

freedom against the labor challenge. Wartime economic planning had rendered the state itself as the largest threat to entrepreneurial freedom. Moreover, under the pressure of the exigencies created by the war the state elites had turned to the leaders of organized labor for support in calming the discontent working class. Business had thus lost its erstwhile ally: the authoritarian state.

The paramount political concern of business throughout the war had been to prevent the limitations on entrepreneurial freedom that had been introduced during the war being made permanent after the war. These encroachments took many forms: the labor-integrative institutions established by the Auxiliary Services Law undermined the traditional ‘master-in-my-own-house’ approach of the heavy industrialists. Price ceilings, import and export controls, state allocation of raw materials and the forced closure of strategically non-essential factories all fundamentally undermined entrepreneurial freedom.

In addition to this, a new threat suddenly emerged toward the end of the war: the threat of a social revolution, amplified by the possibility of a disorderly demobilization, with about 10 to 12 million soldiers returning back from the front within a very short period of time. As a consequence, a large pool of persons that was armed and likely to be unemployed, frustrated, and politically disoriented had to be expected. In this situation, German business conducted a dramatic about-face and discovered organized labor as a valuable ally. An ally needed to organize an orderly demobilization and to stem the threat of a social revolution.

4. II The Post-War Situation: Revolution and Uncertainty

In November 1918 German business and labor reached an agreement that fundamentally restructured the political economy of Germany. In this agreement, known as the *Stinnes-Legien agreement*,⁷³ German industrialists agreed to recognize labor unions as the legitimate representatives of the working class. Moreover, they also accepted the general introduction of collective bargaining agreements and other institutions of cross-class cooperation, like labor exchanges and arbitration committees both on the basis of parity representation, as well as the discontinuation of their financial support to yellow unions and the introduction of the eight hour working day (see Tänzler 1929: 144-145 for a full list of concessions see below).

This class compromise reflected a remarkable change in position by German industrialists concerning their relationship to organized labor: away from the confrontational attitude prevalent before the war, towards the accommodation of labor demands. The

⁷³ Alternatively, the Stinnes-Legien agreement is also frequently referred to as the *November agreement* or *ZAG agreement* or even as the *Magna Charta of Labor*. The term Stinnes-Legien agreement refers to two of the leading participants in the negotiations.

concessions made by business to labor in the Stinnes-Legien agreement were major ones, considering in particular that before the war most German industrialists had resolutely refused to recognize, let alone to collaborate with, organized labor. It is hardly possible to understand how this agreement came about without understanding what motivated industrialists to sign this agreement.

In principle, one can think of two possible alternative explanations. One possible explanation is that the radical about-face in industry's position may have been the result of *a change in preferences* in regard to what kind of political-economic institutions German industrialists considered as best suited to the production strategies they intended to pursue. Such a change in preferences may possibly have been caused by long-term structural changes in the composition of the German business community and facilitated by its strong tradition of corporatist organization and self-government.⁷⁴ In this view, World War I and the political-economic uncertainty that followed served merely to speed up the largely predetermined development towards labor integration (see e.g. Abelshauser 1984: 312).

Alternatively, the about-face may have been the result of a strategy of *political accommodation*, made necessary as an adjustment to a particular historical situation, the war and the ensuing revolutionary situation, which confronted German industrialists with a radical shift in the balance of power and unprecedented uncertainty about its future (Kocka 1984: 72-73). This uncertainty required a radical change in strategy in order to secure entrepreneurial freedom and private capital ownership.⁷⁵ The first explanation emphasizes long-term structural changes, the second contingent historical events.

The empirical analysis in the following section supports the second explanation. On the basis of a detailed analysis of statements by employer representatives the analysis shows that a specific historical situation characterized by extraordinary political uncertainty, unrelated to structural changes in the German economy, motivated German industrialists to fundamentally reconsider their position towards organized labor and class collaboration at the end of World War I. The reorganization of the economy by the state during the war, the imminent defeat and the looming social revolution all together created a situation of extraordinary uncertainty over the future political-economic order, whereby the continuation and, even more so, the aggravation of government controls over the economy appeared as a

⁷⁴ Long-term structural changes are emphasized in particular in (Feldman 1976: 340) , while the importance of pre-war tendencies of corporatist organization are emphasized in (Abelshauser 1984: 298)

⁷⁵ The importance of the revolution is emphasized in particular by Rosenberg (Rosenberg 1977: 278) and (Kocka 1984: 72-73)

very realistic threat. To ward off this threat industrialists were seeking a strategic alliance with organized labor.

Towards the end of the war, major German industrialists started to actively seek the collaboration of organized labor. Their motives for doing so were decisive in making the Stinnes-Legien agreement possible. These motives, however, were the product of the specific historical situation that German industry was confronted with at that moment in time. A situation that was determined by a fundamental uncertainty about the future shape of Germany's political-economic order. This uncertainty resulted from the imminent military defeat and the ensuing breakdown of the old authoritarian political regime. Throughout the war German industrialists had hoped that a military victory and annexations would strengthen the popular legitimacy of the authoritarian monarchy, thereby allowing a return to the *status quo ante* of a non-interventionist political-economic order. In October 1918, German industrialists were caught off guard by the rapid course of events and suddenly found themselves to be dependent on the willingness of organized labor to collaborate in order to stabilize the situation and prevent their expropriation. Leading industrialists realized that an orderly demobilization and a well-organized transition from war-time to peace-time economy would be essential to stem the threat of social revolution and Bolshevism. An orderly and smooth transition though could only be achieved in collaboration with organized labor, because the state bureaucracy appeared no longer capable of organizing this transition in an effective way.

The German November Revolution 1918

Uncertainty over the future political-economic order culminated in the events of November 1918, which became known as the so-called 'November revolution'. This revolution was decisive for bringing about the Stinnes-Legien agreement and its main events are therefore briefly discussed in this sub-section. The revolution consisted of a series of subversive events and upheavals that culminated on November the 9th, 1918. It led to the forced abdication of the Emperor on that day and ended, eight months later, with the establishment of a parliamentary republic based on universal suffrage for men and women. The revolution was not controlled or orchestrated by a single party or organization, but was, instead, the result of the chaotic actions of several groups and parties that were pursuing partly conflicting political goals. At the time the revolution took place it was far from clear that the outcome would be a capitalist order based on a parliamentary democracy, nor were the political goals pursued by the revolutionary groups entirely clear.

The key actors in the revolutionary events were (a) the representatives of the old regime, (b) the political leaders of the Majority Social Democrats (SPD) and the social democratic labor unions, and, in opposition to SPD and union leadership, (c) the revolutionary “worker councilor movement”, an unguided grass-roots movement that had emerged spontaneously all over Germany during the last days of the war, consisting mostly of workers and returning soldiers. The councilors were supported by the Independent Social Democrats (USPD), a political party that had emerged as a secession from the SPD (subsequently called the Majority Social Democrats) during the war.

The revolution took its starting point when at the end of October 1918 sailors on board of two battleships refused to obey orders (Carr 1979: 248). During the following days the revolution spread quickly throughout the country and the emerging movement of ‘workers’ and soldiers’ councilors’ were demanding control over state authority all over Germany (Carr 1979: 250). Events culminated on November the 9th in Berlin. Workers had left the factories and were demonstrating on the streets (Carr 1979: 250). The SPD leadership, headed by *Friedrich Ebert*, feared a radicalization of the revolution along the lines of the Bolshevik revolution that had taken place just one year earlier in Russia, spoiling the prospects for a more orderly, reformist transformation of the political regime. On November the 7th, SPD leader Ebert declared that ‘If the Kaiser doesn't abdicate the social revolution is unavoidable. But I don't want it, indeed I hate it like the sin’ (Baden 1968: 599f.). On November the 9th the Emperor abdicated⁷⁶ and his Chancellor, *Prince Max von Baden*, surrendered his position to Friedrich Ebert, the SPD leader. On the same day, *Karl Liebknecht*, the leader of the revolutionary *Spartacist League*⁷⁷ proclaimed Germany to be a Socialist Republic:

Party comrades, I proclaim the Free Socialist Republic of Germany....; in which there will be no more servants, in which every honest worker will find the honest pay for his work. The reign of capitalism which has turned Europe into a field of corpses is broken. (quoted in Michalka and Niedhart 1992: 21)

The SPD party leadership was trying to calm the mood and to take the sting out of the revolutionary movement. Under pressure, it also proclaimed a republic and declared to form a ‘workers’ government’ headed by Ebert. The SPD leadership was thus acting in opposition to the USDP and the revolutionary worker councilors. Both sides were claiming to be in control of state authority. In order to calm the revolutionary forces and to give more legitimacy to the

⁷⁶ On that day the Emperor had fled to the Netherlands, meaning that, in effect, though not officially, he had abdicated.

⁷⁷ The Spartacist League constituted the left-wing within the USDP and later transformed itself into the Communist Party

new government he intended to form, Ebert offered the USDP half of the seats in the new government. The USDP accepted but insisted on a number of concessions. Only Socialists, no conservatives or liberals, should be included in the new government. Moreover, the government had to declare that all power resided ultimately with the revolutionary workers' councilors and that the government exercised power only in their name; and finally, the elections to the new republic's constituent assembly should be delayed until the revolution was consolidated. The last point was of particular importance because the USDP was aiming at a nationalization of key industries. By delaying the constituent assembly, the USDP had hoped to be able to achieve a quick nationalization that would face the assembly with unchangeable facts.

The provisional government that was formed on November 10th, the Council of People's Deputies ("Rat der Volksbeauftragten"), consisted of three Majority Social Democrats and three Independent Social Democrats and acted on behalf of the revolutionary workers' councilors (Carr 1979: 254). This ambiguous compromise, a socialist government acting on behalf of a revolutionary movement but headed by a moderate reformist (Ebert), reflected the uncertainty at that time over the future path Germany would take. The historian Rudolf Coper, for instance, remarked:

Ebert was faced with a dilemma. The first proclamation he had issuedbegan: 'The outgoing Reich Chancellor, Prince Max of Baden, has ... transferred upon me the administration of the office of Reich Chancellor. I am about to form the new government in agreement with the parties and shall report to the public forthwith!' (...)Twenty-four hours later Ebert became a People's Commissar and acknowledged that the political power resided in the workers' and soldiers' councils. Germany was, in fact, a soviet republic. (Coper 1955: 102)

Supported by a new constitution and, in particular, the introduction of universal suffrage for men and women,⁷⁸ the Majority Social Democrats were confident of gaining an electoral majority through parliamentary elections and thus thought themselves able to implement their reformist programme within the framework of a parliamentary democracy. The USDP, in contrast, supported the revolutionary councilor movement.⁷⁹ The revolutionary worker councilors also lacked a unified political programme or ideology and many of them were, in fact, social democrats. The workers' councilors had emerged at the local level as a spontaneous outburst of political discontent and did not have any centralized decision-making

⁷⁸ Hitherto, universal suffrage existed only for men.

⁷⁹ The USDP, founded in April 1917, had emerged from a split within the SPD about the party's support for the war credits and the 'sacred truce' policy. The USDP was primarily united by its firm anti-war stance, while it did not have a uniform political programme or ideology. The founders of the USDP included the more moderate 'revisionists' *Eduard Bernstein* and *Karl Kautsky* as well as the revolutionary Spartacist League, led by *Karl Liebknecht* and *Rosa Luxemburg*, who later founded the German Communist Party (KPD).

structure. Their political priorities were to end the war and democratize the political system. Demands for the nationalization of heavy industry were raised by the worker councilors and also circulated widely within SPD and USDP.

Many worker councilors wanted to go further and establish “direct democracy” in the factories, resulting in the ‘self-administration of the economy by the working class’ (Müller-Jentsch 1986: 218; Maier 1975: 138). Elected worker councils should take over control at all political levels in the form of a ‘council republic’, a government by soviets, inspired by the Russian model. The economy and political system would both be governed by worker councilors. The leaderships of SPD and social democratic unions wanted to prevent such a Council Republic because they believed in the superiority of a piecemeal, reformist strategy. The anxiety about the possible consequences of a socialist revolution was shared by the leaders of the social democratic labor movement and the leaders of industry and, therefore, formed the common ground upon which the Stinnes-Legien agreement could be built.

4. III The Stinnes-Legien Agreement: Class Collaboration in Uncertain Times

In the context of this uncertainty about the future political-economic order of Germany, a group of big industrialists and labor union leaders joined forces to engineer a far-reaching class compromise that established an institutional basis for cross-class cooperation. The agreement was engineered in October and November 1918; and signed on November 15th, 1918, six days after the outbreak of the revolution. These big industrialists had reversed their attitude towards cooperation with organized labor and were now actively seeking cross-class collaboration. The motives for this about-face were rooted in the political and economic uncertainty of that time. Industry had been seeking the collaboration of organized labor, initially, for the purpose of jointly organizing the demobilization, the re-integration of returning soldiers into the firms, in order to thereby secure a smooth transition from war-time to peace-time economy. An orderly and smooth demobilization was necessary for avoiding a collapse of economic production and mass unemployment, and was thus considered by industry as crucial for avoiding a social revolution. However, due to the imminent collapse of the old political regime industry could not rely on its pre-war ally, the state, in organizing an orderly demobilization, and decided to resort to organized labor instead.

Up to the summer of 1918, German industry, with few exceptions, had rejected union proposals for cooperation in the organization of the post-war economy. Already at the beginning of the war labor union leaders had called upon employers to form joint working

committees (*Arbeitsgemeinschaft*), but these calls were left unanswered in most sectors. Such working committees⁸⁰ were established in those sectors where negotiations had already been taking place before the war, in particular in construction, printing and timber (Reichert 1919: 5), while the heavy industry in particular maintained its traditional anti-union stance (Feldman 1976: 323; Schönhoven 1987: 254). The official position of the employer associations toward cross-class collaboration remained negative throughout the war (Kocka 1984: 69). The initiative for cross-class collaboration came originally not from industry but, instead, from an impulse from outside.

This outside impulse came from August Müller, a state secretary who had good contacts to union representatives, and Hermann Schumacher, a political economist and academic social reformer who had good contacts to industry. In May 1917 these two men initiated talks between employer representatives, led by the heavy industrialist Hugo Stinnes, and union representatives, led by Carl Legien (Leckebusch 1966: 71; Feldman 1976: 323-324). These talks, however, collapsed in October 1917 because unions could not consent to the employers' demand that they should declare their political support for a strategy of military annexations, a strategy that had been at the core of a plan by the Fatherland Party and industrialists to re-unite the population behind the war effort (Feldman 1976: 324). At that time, future developments appeared apparently too uncertain for both sides and no side was prepared to make the kind of concessions that would have been needed to forge a cross-class alliance.

Negotiations between capital and labor at the national level did not resume before October 1918. Already some time before, in January 1918 *Hans von Raumer*, the executive director of the Association of the German Electric Engineering Industry, took the initiative for talks between employers and unions in his sector. Raumer was realistic about Germany's military situation, and feared that, unless the cooperation of organized labor in the organization of the post-war economy could be won, political chaos and continued government control would be the consequence (Raumer 1955, 1954). Raumer sidestepped the leading business associations on the grounds that their clumsy organization made them unable to change their official positions without lengthy debate.

Instead, Raumer decided to consult with individual industrialists, most of them from the manufacturing industries: *Carl Friedrich von Siemens* (electric engineering), *Walter Rathenau* and *Felix Deutsch*, both from the electric engineering firm AEG, *Reichsrat von Rieppel*, the executive director of the machine building firm MAN, and Hugo Stinnes, the

⁸⁰ These committees dealt in particular with job placements for war-disabled persons.

reform-oriented heavy industrialist already involved in the May 1917 talks (Raumer 1954: 428-429). These persons formed the core of the employer group in the negotiations with the unions. All, except one, were representatives of the manufacturing industries and were critical of the conservative political views that dominated in the heavy industry. The most severe opponents of cross-class collaboration were thus sidestepped by Raumer and his collaborators, though the associations of the heavy industry agreed to sign the agreement *ex post* (Raumer 1954: 428; Reichert 1919: 11 for the list of signatory associations).

Raumer's initiative did not, however, initially find much support among industrialists in other sectors. Remarkably, the first meeting with union representatives did not take place until October 2nd, 1918 (Leckebusch 1966: 71; Raumer 1954: 428). Up to the autumn of 1918, dominant groups among German employers apparently resisted negotiations with unions. This is evident from a memorandum published by the VDA in March 1918, in which the federation elaborated its ideas for the organization of the peacetime economy. This memorandum included no space for institutions of cross-class collaboration. The memorandum opposed any intervention into entrepreneurial freedom by the state or the unions. It demanded the dismantling of the measures of 'wartime socialism', in particular the works councils and parity-based arbitration boards, and demanded the re-establishment of a free market economy after the war:

An emergency law, necessitated by the exigencies of war, is in particular the War Auxiliary Services Law, for the continuity of which there is obviously no reason after a peace agreement...To be sure, also *the institutions created by the law are dispensed with*. This holds in particular for the arbitration committees and arbitration boards... (VDA memorandum from March 1918, quoted in Leckebusch 1966: 68, translated by TP, emphasis by TP)

The looming military defeat and the uncertainty about the future political-economic order motivated German employers to reconsider their position towards organized labor and its demands. Cooperation with organized labor was now the lesser evil compared to the revolutionary threat posed by the political radicalization of the unorganized worker masses. Employers recognized that a cross-class collaboration would only be possible if they were to make concessions to organized labor. The executive director of the Association of German Iron and Steel Industrialists, Jacob Reichert, argued in the autumn of 1918:

It is clear that the industrialists want to win the workers and their organizations for a common industrial policy, which can only be achieved if we offer a service in return for the assistance that we expect from the employees. And this return service had to consist [in the past, TP] and will have to consist in concessions in social questions, in particular regarding working conditions. That is the big sacrifice that entrepreneurs have made and will have to make. This is not only a financial sacrifice, but, I believe, for some industrialists also a difficult sacrifice

in terms of conviction, given that, up to recent months, they have refused to negotiate with organizations that represent only a small faction of the workforce, but nevertheless would like to be seen as the legitimate representatives of the entire workforce. But what's the use of this anyhow? The sacrifice has to be made. And further sacrifices will have to be made in the future, because of economic necessities and also political necessities (Reichert 1919: 7, translated by TP).

Reichert was thus fully aware of the power and the influence that the labor unions held over the working class and that therefore finding an agreement would be unavoidable, even though this would be painful. Cooperating with the unions was a delicate issue for the employer associations, which only a few years earlier had refused to even recognize unions. How problematic the issue was for the employer associations is evident in the fact that the agreement was not engineered by the employer associations themselves, but became possible only as a result of the personal initiative of a small group of individual industrialists and industry representatives. These people did not act upon a mandate from their associations, but did so only in their personal capacity (Raumer 1954: 430). The peak-level federations of employers and labor unions ratified the agreement *ex post*, only after the negotiations were already concluded.⁸¹

The terms of the Stinnes-Legien agreement

The reversal of industry's position towards labor from confrontation to collaboration reflects the changing balance of class power created by the political uncertainty that resulted from the revolutionary situation. The reformist labor unions became a pivotal ally for employers in their fight against chaos and revolution. While it took eight months for the talks to get started after Raumer had taken the initiative in January 1918, events began to proceed very fast from October on. The first round of negotiations took place on October 22nd, 1918. Already on November the 6th, the group presented to the government a plan for a demobilization programme and on November the 15th, the events of November the 9th had in the meantime further aggravated the political situation, both sides ratified the agreement that became known later as 'Stinnes-Legien agreement'⁸² (Reichert 1919: 9). The agreement provided for a joint working committee for the permanent cooperation between capital and labor, the '*Zentralarbeitsgemeinschaft*' (ZAG), as well as the following list of specific concessions to

⁸¹ The members of the negotiation team included in addition to von Raumer, who chaired the negotiations, on the employer side: von Siemens and his company director Henrich, Rathenau (AEG), Deutsch (AEG), Rieppel (MAN, machine building), von Borsig (VDA), Vögler, and Stinnes; on the union side: Legien, Bauer, Eisner, Leipart Harmann, Schlicke, and Stegerwald (Reichert 1919: 8). The majority of these industrialists came from mechanical and electric engineering firms, while the hitherto powerful heavy industrialists were apparently sidestepped, as mentioned above.

⁸² Alternatively, the agreement is also known as 'November agreement' or as 'ZAG agreement' and sometimes even referred to as the 'Magna Charter of Labor'. The original text of the agreement is reprinted in Leckebusch 1966: Appendix 10 (p.224 – 226).

the unions (the original text of the agreement is reprinted, inter alia, in Reichert 1919: 21-22; see also Tänzler 1929: 144-145; as all as Weber 1954: 117-118).

1. Recognition of the labor unions as the legitimate representatives of the workers
2. No limitations to workers' freedom of association
3. Employers will refrain from supporting 'yellow unions'
4. Demobilized soldiers have a right to return to the firm where they were employed before the war
5. Joint administration of labor exchanges based on parity representation of capital and labor
6. Wages and working condition have to be regulated by *collective agreements*, organized on a sectoral basis
7. *Worker committees* for all firms with more than 50 employees, to represent the interests of the workforce and monitor the implementation of the collective agreements in cooperation with the entrepreneur
8. Formation of parity-based arbitration committees by collective agreements
9. *Eight hours working day*, without concomitant wage reductions, but conditional on other countries doing the same
10. Formation of a new body (the ZAG), to implement this agreement and to organize the demobilization, based on parity representation
11. Decisions made by the ZAG are binding for both sides.

These were very major concessions by business to labor, motivated by the aim to guarantee an orderly demobilization with the help of union collaboration and thereby avoid a social revolution. The agreement was supported by the new socialist government and its main components were transformed into law.⁸³ According to Raumer's own recollection, there was not much debate about the demands made by the labor unions, except notably the abandoning of the yellow unions and the introduction of the eight hour working day (Raumer 1954: 428; Reichert 1919: 12-13; Erdmann 1966b: 90-103). Fearing that the socialist government would

⁸³ The Weimar constitution, passed on August 11th, 1919, which founded the Weimar Republic, removed the remaining limitations on the freedom of association and recognized labor unions and employer associations (Art. 159 of the Weimar constitution). The organizations of employers and workers were legitimised to negotiate wages and working conditions; collective agreements had to be respected by the state (Art.165). Already in November 1918 the government issued an ordinance regulating working time. In December 1918 an ordinance was passed, which established on a provisional basis wage agreements, works councils and arbitration boards (Tänzler 1929: 154). The ordinance established in particular the 'indispensability' ("*Unabdingbarkeit*") of collective agreements, meaning that collective agreements cannot be amended by agreements between the individual worker and his employer, except to the advantage of the worker. Thus, collective agreements were effectively established as creating a minimum wage standard. In addition, the ordinance also introduced the 'declaration of general applicability', i.e. a possibility for the Ministry of Labor to declare collective agreements as being generally binding for all firms and all workers, including those not organized in employer associations and unions. Indispensability and general applicability were both accepted by employers (Weber 1954: 121). The ordinance also prescribed works councils for all undertakings with at least 20 workers as well as parity-based arbitration institutions for the settlement of labor disputes. The Works Council Act passed by the parliament in January 1920 turned the works councils into a permanent institution (see below). Most of these rules and principles enshrined in these laws and decrees, indispensability, general bindingness and works council, are still part of the industrial relations institutions in Germany today. Public arbitration boards with power to make binding decisions, though, did not survive the Weimar Republic.

foist the eight hour working day upon business by law, industry eventually decided for a voluntary agreement:

The eight hour working day is one of the most long-standing demands of organized labor. With a revolutionary government, consisting only of workers, one had to suspect that in the absence of a concession by the entrepreneurs, the eight hour working day would be introduced by law. A voluntary agreement is, without doubt, worth twice as much as to push one's luck for a compulsory regulation. (Reichert 1919: 12, Reichert was the executive director of the Association of German Iron and Steel Industrialists)

Remarkably, the agreement consisted only of concessions by business to labor, and no explicit concessions by labor to business. Why have German industrialists signed an agreement that extorted only concessions from them? Clearly, what these industrialists were seeking was the willingness of organized labor to collaborate with employers on the crucial issues of organizing demobilization and the transition to a peace-time economy,⁸⁴ and thereby colluding with capital in warding off a social revolution. Both sides declared that they 'are resolved to work together in unity concerning all questions pertaining to the demobilization and transition from a wartime to a peacetime economy' (demarche by unions and employer to the Reich Chancellery, October 30th, 1918, quoted in Feldman 1976: 332-333 , translated by Feldman).

Remarkably, though, the agreement did not touch upon the issue of nationalization of key industries, an important demand of the social democratic labor unions, one which they also shared with the revolutionary councilor movement. By accepting the agreement, the labor unions had achieved recognition and institutional integration.⁸⁵ But they had also effectively impeded their aim of nationalizing key industries, notably the heavy industry. It is understandable, therefore, that the social democratic unions presented the agreement as being a mere intermediary step towards their eventual goal, the socialization of the economy. In November 1920, the Federation of Social Democratic Unions (ADGB) declared that the ZAG would be 'a useful tool in the struggle over the conquest of economic power and the socialization of the economy. Its importance is limited in time and it will cease, as soon as ...other organizations are built that integrate workers into the control of the economy' (quoted in Erdmann 1966b: 108, translated from German by TP).

To sum up, the Stinnes-Legien agreement reflects a massive shift in the position of German employers towards organized labor, from confrontation and repression towards

⁸⁴ This willingness to collaborate with business is clearly implied in points 10 and 11 of the agreement.

⁸⁵ The agreement was signed by the social democratic, as well as the Christian labor unions.

negotiations and compromise. In a retrospective on the ZAG published in 1955,⁸⁶ Hans von Raumer, the initiator of the talks, remarked that '[s]even entrepreneurs, without any mandate by their associations, had made the decision that revolutionized the relationship of the entrepreneurs to the unions' (Raumer 1955, translated from German by TP). The VDA executive director Gerhard Erdmann, had in retrospect stated the ultimate purpose of the agreement clearly: 'These men have the historic credit to have contributed considerably, through their personal courage, towards keeping chaos and a Bolshevist revolution from the German Reich' (Erdmann 1966b: 99, translated from German by TP). In short, the goal of the industrialists that forged the agreement was to pacify the working class with the assistance of moderate labor union leaders.

4. IV Class Collaboration as Social Pacification: Employers' Motivations

To understand how the revolutionary situation induced industrialists to change their mind it is important to look at the timing of the negotiations. The Stinnes-Legien agreement was not the result of a long-run process of rapprochement between capital and labor but, to the contrary, of a sudden about-face. Before October 1918 German industry in general presented itself unwilling to make concessions to organized labor and, with few exceptions, refused to accept collective bargaining and institutions of class cooperation and conciliation. Throughout most of the war period, German business representatives were adamant that the institutions for class conciliation introduced by the Auxiliary Services Law (worker committees at the workplace and parity-based arbitration boards) would not be allowed to serve as a precedent for the organization of the post-war economy (see section I above). For most of the war period, industry remained unwilling to make the kind of concessions that would have opened the way for class collaboration. Only once the revolutionary challenge became manifest did industrialists develop a strong commitment to class compromise.

Talks between industrialists and labor union leaders had already begun in 1917 but had initially come to naught. Up to the summer of 1918 no discernible progress was made in class rapprochement, while in contrast events started to happen very fast during the final weeks of the war, when Germany's defeat was imminent. Negotiations between union leaders and industrialists started on October 22nd, 1918, the agreement was signed only three weeks later, on November the 15th, 1918 (Raumer 1954: 428-430). This rapid speed-up of events

⁸⁶ The text is a speech written by Raumer in the 1950s by order of the public broadcasting station WDR, which produced a radio documentary on the genesis of the Stinnes-Legien agreement. The fact that this major public broadcaster produced a documentary on the Stinnes-Legien agreement underlines the importance given to this agreement in Germany. Raumer's speech was reprinted by the BDI in 1955 (Raumer 1955).

points to the crucial importance of uncertainty about the future political-economic order in compelling industry to accommodate organized labor. By signing an agreement with the unions, they intended to reduce the uncertainty about the future path Germany would choose. Even in July 1918, Hans von Raumer, the initiator of the agreement, still had to urge his colleagues to resume talks to form an ‘organic collaboration with the unions...before the flood of events overcame us all’ (Raumer 1954: 428-429). The purpose of this section is to present further archival evidence confirming the importance of social pacification in the motivations of industrialists to make concessions to organized labor.

On October 9th, 1918 German iron industrialists met in Düsseldorf to discuss what to do to prevent revolution and nationalization. The participants of the meeting mandated Hugo Stinnes to negotiate with organized labor (Reichert 1919: 7) but did so with apparently mixed feelings. The participants were completely clear that an alliance with organized labor would be the only way to stabilize the political situation and to ward off nationalizations and a social revolution (Reichert 1919: 6). Though the labor unions had lost strength in the early years of the war, due to the conscription of many of their members, they had experienced a rebound in their strength after the passing of the Auxiliary Services Law (see chart 4.1 above). Therefore, they could potentially serve as a strong ally for business against the revolutionary challenge, if their cooperation could be won:

What was important was: How can one rescue industry? How can...the entrepreneurs be saved from socialization...and the approaching revolution? (....) The assembled were unanimous in feeling that the government of Prince Max von Baden ...was untenable under the existing circumstances and that it would soon be brought down. In any case, the iron industrialists could expect no help from a weak government. *Only organized labor seemed to have the commanding influence*. From this fact the conclusion was drawn that, in the midst of general great uncertainty, the failing power of the state and the government, industry could only find strong allies in the labor camp, and they are the unions (Reichert 1919: 6 emphasis added by TP).

At that time, German heavy industrialists were thus fully aware of the crumbling authority of the old political regime and accepted the need to make sacrifices to organized labor in order to gain the desired union assistance in social pacification. Industry did not trust the authorities of the old political regime to be capable of organizing an orderly and smooth demobilization and, hence, decided to resort to organized labor, the only actor that had sufficient credibility among the demobilized soldiers and munition workers to secure calm and order. Consequently, the organization of a joint demobilization programme was the top priority for business. The demobilization had to be conducted with great speed in order to evacuate enemy territory in time, care had to be taken for the employment of the returning soldiers, food supplies needed to be organized, allocation of raw materials needed to be

rearranged, et cetera. Failure to do so would have resulted in millions of returning soldiers without employment and income: industrialists feared a large mass that was armed, politically discontent, and disoriented. Director *Henrich* of the *Siemens*⁸⁷ group pointed out the dangers created by an ill-prepared demobilization in a speech given to colleagues:

A poorly prepared demobilization will bring revolution and the destruction of industry and our economic life by our own people. A poorly prepared final struggle will bring defeat and the destruction of our industry by our own soldiers and the foreign troops streaming after them. (Director Henrich of Siemens speaking at a meeting of the German Society of Engineers, October 20th, 1918, quoted in Feldman 1976: 329, emphasis added by TP).

Privy Councilor Hilger, the Silesian heavy industrialist, who had previously belonged to the most adamant opponents of concessions to organized labor, responded with enthusiasm to the Stinnes-Legien agreement, which he considered as being ‘far more favorable’ than he had expected:

Gentlemen, I stand before you today a Saul transformed into a Paul. Today we cannot get on without negotiations with the unions. Yes, gentlemen, we should be happy that the unions still find themselves ready to deal with us in the manner in which they have, for only through negotiations with the unions, through our agreement with the unions, can we prevent - call it what you will - anarchy, Bolshevism, rule of the Spartacists, or chaos (statement by Privy councilor Hilger made at the meeting of the executive committee of the Association of the German Iron and Steel Industrialists on November 14, 1918, quoted in Feldman 1992 [1966]: 528, emphasis added by TP).

The nationalization of industry was clearly the biggest threat that the revolution posed to industry. Hugo Stinnes made this link very clear when he suggested to his colleagues that the agreement he and his collaborators had worked out would effectively avert the risk of nationalizations:

I would urge you to pay as little attention as possible to these things [demands for nationalizations, TP], but take care of this matter [i.e., the agreement] here, for when that is made, then the other will disappear of itself [statement made by Stinnes in a meeting on Nov 14, 1918 quoted in Feldman 1976: 337]

Anxiety about nationalizations and the fundamental political character of the economic order following the revolution clearly took priority over the question of how to organize industrial relations in the new state. Social policy and industrial relations issues were of secondary importance to industry and concessions on these issues served merely as side-payments, used deliberately with the purpose to win the support of the unions. Hans von Raumer remarked ‘*What did a revolution have to offer to the unions at a moment when they had achieved the basic goals of their decade-long struggles through a voluntary agreement offered by the entrepreneurs?*’ (Raumer 1954: 433).

⁸⁷ Note that Siemens himself was part of the negotiating team

Industry's turn to class collaboration should not be mistaken for a conversion in underlying beliefs of industrialists about what kind of political-economic order or what kind of industrial relations system would be economically most efficient. It was a mere strategic adjustment to a dramatically altered context that had eroded industry's previous power position and confronted it with extraordinary uncertainty about future developments. Carl Duisberg of *I.G. Farben*, the leading representative of the German chemical industry and a participant in the Stinnes-Legien negotiations, had candidly confessed how he had managed to come to terms with the new political regime:

From that day when I saw that the cabinet system was bankrupt, I greeted the change to a parliamentary system with joy, and I stand today, where what is at stake is what I consider to be the highest value, namely the Fatherland, behind the democratic government and, where this is possible, *I work hand in hand with the unions and seek in this way to save what can be saved*. You see, I am an opportunist and adjust to things as they are [Duisberg to Dr. E.A.Merck, Oct 17, 1918, quoted in Feldman 1976: 337, emphasis added by TP]

Support among the rank-and-file of both sides towards the new approach was fragile from the beginning and contributed to the demise of cross-class collaboration in the subsequent years. Not all German industrialists were happy about the agreement. The two peak-level federations of German industry, the CDI and the BdI, were both unhappy that their federations had been bypassed and sent a protest to the government declaring that the businessmen involved in the negotiations had no mandate to speak for industry as a whole (Feldman 1976: 334). Leaders of regional associations in Rhineland and Saxony criticized that the far-reaching concessions made would not have been necessary in their provinces, where the situation was calmer, while representatives of smaller and medium-sized firms complained that big industry had offered more than what they would be able to afford, in particular with respect to the eight hour working day (Reichert 1919: 12; Feldman 1976: 334-339). It would thus be erroneous to think that all of German industry would have fully supported the agreement.

The agreement was controversial within the business community, but it became possible because the political uncertainty at that time and the urgency of the matter allowed a group of single-minded industrialists to bypass the usual mechanisms of intra-business consultation and, together with their union counterparts, create a *fait accompli* that also the dissenters were compelled to accept. Once the political situation had become more stable the interest in class collaboration also started to wane. This holds for both sides. Employers tried to retreat on some concessions, in particular the eight hour working day, while unions became more reluctant to collaborate. Ordinances and laws passed by the state had already transferred the concessions made by employers into legally binding rules, making organized labor less

reliant on continued collaboration. The next section looks at the mixed success of class collaboration in practice.

4. V Class Collaboration in Practice: The Erosion of Consensus

The operation in practice of the joint committee set up by the agreement, the ZAG, fell far short of the expectations and its implementation progressed only slowly. It took more than one year for the committee's bylaws to be passed on its constituent assembly on December 12th, 1919 (Berg and BDI 1956: 201). Once the revolutionary moment had receded, employers were trying to retreat on some of the concessions made, in particular concerning the eight hour working. Cooperation within the ZAG started to crumble already in 1920 (Berg and BDI 1956: 202). The committee was finally dissolved in 1924, when the social democratic union federation (ADGB) left the ZAG in response to employers in some sectors unilaterally abandoning the eight-hour working day. The construction and metal worker unions had already left the ZAG in 1922 (Berg and BDI 1956: 203). However, after the ADGB had left, only the Christian Democratic unions remained in the ZAG, in effect condemning the ZAG to irrelevance. Employers became unwilling to sustain the ZAG through concessions to the unions, which resulted in the unions abandoning the ZAG. In short, once the uniting forces of the revolution had disappeared, irreconcilable conflicts surfaced again and both sides returned to their pre-war positions and strategies of class confrontation (Leckebusch 1966: 73).

The Provisional National Economic Council

The establishment of a new institution for corporatist policy-making, the *Provisional National Economic Council* ("Provisorischer Reichswirtschaftsrat"), further contributed to the demise of the ZAG by creating a competing arena for negotiation and compromise, though also this institution remained largely ineffectual. This body was established in April 1920, based on a programme for 'economic democracy' that was advocated by the social democratic Minister of Economics, Wissell, and the social democratic labor unions (Leckebusch 1966: 79; Tänzler 1929: 156). After the social democratic-led government had decided that plans for a nationalization of the heavy industry were premature (Carr 1979: 270), the focus of social democratic and labor union policy shifted to the concept of '*economic democracy*' instead. This concept was based on the idea of democratic self-governance of the economy, based on equal representation rights for workers and employers.

The formation of corporatist bodies of economic governance was envisaged in the Weimar Constitution. According to Art. 165 (3) of the constitution, parity-based consultative

bodies, the 'economic councils', were to be established at all levels of the economy, from the local via the regional up to the national level. While the works councils established labor representation at the level of the workplace, the economic councils would serve a similar purpose at the higher political levels. The *National Economic Council* was supposed to form the peak-level of this multi-level structure of 'economic democracy'. The establishment of the intermediate level bodies did however never occur and the programme got stuck as a result of the intensifying disagreements between capital and labor (Braunthal 1978: 169-171).

The *Provisional National Economic Council* established in 1920 was the only of these corporatist institutions provided in the Weimar Constitution that was actually put into practice. The Council was intended as a 'parliament of the economy', though it possessed only very limited competencies. The limited definition of competencies was the result of a compromise in the constituent assembly between socialist and bourgeois parties (Berg and BDI 1956: 205). Its main competence was to issue non-binding opinions on planned legislation in the field of economic and social policies. The Council was effectively competing for competencies with the ZAG committee and thereby contributed to the demise of the ZAG (Tänzler 1929: 172).

Similarly to the ZAG, the Economic Council also remained a largely ineffectual body. The Council was made up of 326 members that were organized into three groups, employers, workers and other interest groups⁸⁸ (Leckebusch 1966: 79, Fn.214). The size of the body and the inclusion of the third group, the 'others', had both contributed to the ineffectualness of the Council. Finding a majority in the Council was generally difficult. In cases of a conflict between capital and labor, members from the third group often provided the crucial votes for one of the two sides to gain a majority. This reduced the need for capital and labor to find compromises, as each side could hope to find allies for its position from among the third group (Erdmann 1966b: 111; Braunthal 1965: 187).

Despite the eventual failure of the ZAG to establish a body of corporatist governance at the national level, the Stinnes-Legien agreement remains enormously important for the subsequent development of the industrial relations in Germany, because the concessions made by employers were transferred into law. Some of the concessions originally made by business were, however, later withdrawn, in particular the eight-hour working day.

⁸⁸ The third group included, inter alia, academics, consumers, free professions and public authorities

The working time conflict: Withdrawal of concessions

The transformation of the basic elements of the Stinnes-Legien agreement into law meant the institutionalization of the cross-class compromise forged during the revolutionary post-war situation. The public arbitration boards and the eight-hour working day became the main targets of attack by employers. The Stinnes-Legien agreement specified that daily working time should not exceed eight hours. Demobilization decrees had turned this rule into law (Leckebusch 1966: 76). The eight-hour working day did, however, turn out to be at odds with economic exigencies. The effort to rebuild economic production and the obligation imposed on Germany by the Peace Treaties to make reparation payments to the victors, part of these in the form of deliveries of coal, steel and agricultural products, strained the production capacities of the German coal mines and led to a serious lack of coal supply. The coalmining industry responded to this by trying to extend overtime work, an attempt that met with substantial resistance by the coalmining unions (Erdmann 1966b: 136).

In 1922 German heavy industry stepped up its campaign against the existing working time regulations and demanded that they be made more flexible. In October 1923 the peak-level federation VDA issued a memorandum declaring that only a “return to pre-war working times” would allow the economic reconstruction of Germany. After the validity of the demobilization decrees regulating working time had expired, the coalmines exploited the regulatory vacuum and extend working time unilaterally, that is, without the consent of the unions (the so-called ‘Unna decision’).

Attempts by the Social Democratic parliamentary faction to extend the validity of working time regulations did not find a parliamentary majority and, as a consequence, the pre-1918 rules were reinstated. The social democratic-led grand coalition, headed by *Stresseman*, collapsed over the working time issue and the labor unions in 1924 left the ZAG in protest over the unilateral behavior of employers on this issue. In December 1923 the new government, a coalition of non-socialist parties, decreed a new working time regulation that accommodated the demands of the heavy industry for more flexibility. The working day could be extended to 10 hours by collective agreements or by government decree. Subsequently, collective agreements became the basis for working time regulation, strengthening the importance of employer organizations and unions in the regulation of working time (Erdmann 1966b: 135-137).

Works councils

The introduction of mandatory works councils, as institutions for the representation of worker interests at the workplace, was one of the most substantial and durable outcomes of the Stinnes-Legien agreement. As mentioned in section I, mandatory works councils were introduced already by the Auxiliary Services Law in 1916, but at that time were accepted by employers only as a temporary institution, valid for the period of the war only. In the Stinnes-Legien agreement (Point 7), employers accepted mandatory works as a permanent institution. A few months later, employers decided to oppose the Works Council Law passed by parliament in January 1920. In the meantime, the political situation had stabilized sufficiently for employers to recover from the shock of revolution. With their regained confidence, employers tried to withdraw the concession they made only one year before. Employers claimed that the government bill would provide the works councils with too far-reaching competencies, in particular in regard to co-determination rights concerning the hiring and firing of workers and the introduction of new production methods (Berg and BDI 1956: 209-211). Moreover, they suspected that works councils would harm cooperative labor relations by creating a platform for political agitation (Leckebusch 1966: 78-79; Tänzler 1929: 211).

Worker demands for elected representatives at the workplace date back to proposals presented to the revolutionary Frankfurt Parliament in 1849. Already from the 1880s on, precursors of works councils were established by some firms on a voluntary basis. The *Worker Protection Law* (“*Arbeiterschutzgesetz*”) of 1890 recognized works councils as a voluntary option for firms. The Prussian Mining Law of 1905 for the first time established works councils on a compulsory basis, though the law only applied to Prussian coalmines. The War Auxiliary Services Law then institutionalized works councils on a broader basis, albeit only for the period of the war (Leckebusch 1966: 77-78; Thelen 1991: Ch.3). In the Stinnes-Legien agreement German employers eventually consented to works councils as a mandatory institution for the whole economy. In January 1920, the national parliament with a broad majority (215-63) passed a law that institutionalized mandatory works councils (Braunthal 1978: 167-168).

The 1920 Works Council Law (“*Betriebsrätegesetz*”) obliged all firms that permanently employed more than 20 workers to establish a works council. According to the law, the works councils were supposed to fulfill a double function: first, to represent the “common interests of the employees” vis-à-vis the entrepreneur and, second, to support the employer in achieving the “purpose of his business” (§ 1 of the Works Councils Law, adopted by the German National Assembly on January 18th, 1920). Works councils were not allowed

to initiate or participate in strikes and were obliged to cooperate with the employer to 'protect the plant from unrest' (Markovits 1986: 34). Thus, the works councils had to represent labor interests and assist the employer at the same time. The double purpose reflects a compromise between capital and labor, though in practice, works councils limited themselves to representing the interests of workers.

Employers responded to the passing of the law with despair. They feared that the works councils would become a vehicle for political agitation and radicalization among workers (Tänzler 1929: 211; Berg and BDI 1956: 209-211). At the VDA general assembly in 1919, the employer federation issued the bleak warning that 'the introduction of works councils and their prospective competences mean such a deep intervention into the entrepreneur's right to self-determination and responsibility that...a damage to the enterprises and the whole industry would be the consequence.' (quoted in Braun 1927: 46, translated from German by TP).⁸⁹ The implementation of the law was uneven. Some employers refused to comply (Brigl-Matthiaß 1926: 76). They did not set up works councils at all or dismissed councilors that they considered to make undue use of their rights in order to intimidate other councilors and make them quiescent (Guillebaud 1928: 225). Other firms reportedly made positive experiences with works councils and admitted that the initial fears had not materialized⁹⁰ (Erdmann 1966b: 144-145).

⁸⁹Subsequently, the conflict between organized labor and employers focused more on the precise delimitation of the power of works councils, rather than on their existence as such. Employers demanded that works council competencies should be limited to labor issues, while the labor unions wanted the works councils to be involved on all issues of business policy. The law did not specify the precise areas of interests where works councils would be entitled to act, except for declaring that the works councils had a right to veto dismissals. The conflict over works councils competencies involved in particular the implementing regulations that defined the rights and competencies of works councils. In February 1921 an implementing regulation obliged firms to present their balance sheets to their works council. One year later, works councils became entitled to be represented as a minority group in the supervisory boards of firms (Fürstenberg 1978: 2). The competencies of works councils where, thus, extended far beyond social issues into economic issues, that had hitherto been the prerogative of the entrepreneur. (Erdmann 1966b: 139-146).

⁹⁰ The following statements from the mining industry illustrates the changing attitude towards works councils: 'In retrospect, after three years of practical experience with the works councils, one can definitely make the satisfying statement that the Works Council Law, which was initiallyseen as a wedge [separating capital and labor] harming labor peace and as a cause of economic decay, has become a tool for the stabilization of labor peace and the rapprochement between employer and employees,..., [that is]not to be sneezed at. Today, one can make the pleasant statement that one has been mistaken and that the great mass of German people take a much more realistic and reasonable ['wirtschaftsvernünftig'] position on economic issues than what one had dared to hope, [and] that the revolutionary and councillor movements of the initial demobilization period was merely the consequence of a not very dramatic fire blight that was raked by foreign ideas' (Deutsche Bergwerkszeitung, No.28, 1923, quoted in Erdmann 1966: 145, translated from German by TP).

Conclusions

The Stinnes-Legien agreement is a case of strategic cross-class collaboration, motivated by the goal of industrialists to pacify the population with the assistance of pragmatic labor union leaders. The concessions made in this agreement have shaped the institutions of German industrial relations up to the present, most importantly the works councils and rules for sectoral collective bargaining. The agreement was, first and foremost, an *ad hoc* response to the threat of a socialist revolution, which united employers and union leaders, rather than the product of foresighted industrialists trying to design economically efficient labor market institutions. Class cooperation in the ZAG committee collapsed after a few years. Employers retracted from major concessions once the political situation had stabilized, most importantly the eight-hour working day, resulting in the collapse of institutionalized cross-class collaboration in 1924. With the containment of the revolutionary movement, the goal of social pacification lost relevance.

During most of the war period, like before the war, the vast majority of German employers refused to negotiate with labor unions and viewed their reformist demands as the main threat, rather than the political radicalization of the unorganized working class. Only as late as autumn 1918 did key segments of German industry change their mind. They did so to prevent a social revolution and a further intensification of state interventionism. What had changed, compared to before the war, was the role of the state, both its actual and its anticipated future role. Before the war, employers could rely on the government as their ally against organized labor. The pre-war German state took a non-interventionist position on economic issues and, even after abolishing the anti-socialist laws in 1890, was trying to repress the socialist labor movement by various means. The war changed this. The army turned to organized labor for assistance in order to sustain popular support for the war effort. At the same time, entrepreneurial freedom became highly restricted by war-time economic planning. German business was left without a reliable ally. The war had alienated industry from its old ally, the government, and, at the same time, had turned organized labor into a more respectable force in the view of industry.

The sudden change of mind by German employers was an attempt to reduce the extraordinary uncertainty about Germany's future political-economic order through a negotiated compromise with the unions. The collapse of the old regime and the revolutionary threat made the big industrialists politically powerless and dependent on the cooperation of

the unions to build a bulwark against a socialist revolution.⁹¹ Industry feared the collectivization of industrial ownership and a massive intensification of state interventionism if the revolution would succeed. The revolutionary movement receded after the initial post-war period and the Weimar system of parliamentary democracy showed first signs of stabilization. At the same time, also cross-class collaboration began to crumble. After heavy industry employers had unilaterally annulled the eight-hour working day in 1924, the labor unions withdrew from the ZAG, meaning the collapse of this form of institutionalized cross-class collaboration. Several attempts in the coming years to reinvigorate the ZAG failed. In the absence of a unifying challenge, the political mood had started to turn toward class polarization again.

This chapter has tried to show that strategic accommodation to a situation of extraordinary political and economic uncertainty is better able to explain the Stinnes-Legien agreement than a genuine preference of German employers for cultivating social compromise. The latter interpretation is suggested, for instance, by an argument presented in Cusack, Iversen and Soskice (2007: 377-381). According to these authors, employers relying on so-called asset-specific skills should be expected to actively seek and cultivate institutions of cross-class cooperation and collaboration. Cusack et al. use the Stinnes-Legien agreement and the ZAG as an example illustrating the validity of their argument (Cusack et al. 2007: 380). The fragile and short-lived character of cross-class collaboration in the ZAG does, however, not fit the expectation of a genuine employer preference for social compromise, neither does the development of collective bargaining before World War I (see chapter 2). Moreover, as this chapter has shown, the historical sources do not provide any evidence that issues of skill formation would played a role in employer deliberations leading to the agreement. Instead, these deliberations were overwhelmingly dominated by fears of a social revolution.

The institutions and policies created by the Stinnes-Legien agreement were mere concessions to the labor unions, rather than a reflection of genuinely held preferences by industrial employers. They were not the result of far-sighted industrialists trying to design a

⁹¹ The historian Arthur Rosenberg had remarked about the Stinnes-Legien agreement that ‘The great industrialists were now just as powerless as the feudal class which had ruled Germany until 1918’ and that ‘They were ready to accept anything if only they could keep their property’ (Rosenberg 1977: 278, translation taken from Feldman 1976: 336). Arguing in a similar way, the German historian Jürgen Kocka has emphasized that the ZAG “was probably the strongest bulwark against extreme revolutionary change’ (Kocka 1984: 161). German employers had come to accept collective bargaining, works councils and cooperation with unions in the face of an imminent social revolution. Though collective bargaining had already been accepted by a few sectors on a voluntary basis before the war (see chapter 2) it took the threat of a social revolution to eventually make a national cross-class agreement possible.

modern production regime in line with the production requirements of their firms. They were motivated by the goal of winning the collaboration by the labor unions in organizing economic demobilization and pacifying the population. Industry's consent to collective bargaining and other institutions for cross-class conciliation, I argue, has not been supported by a conversion in beliefs and preferences about what kind of industrial relations system would be most beneficial for organizing industrial production, but was an accommodation to the temporary political weakness of industry.

It is revealing to note that already one month after the signing of the agreement Hugo Stinnes started to fund a precursor of the Nazi movement (Feldman 1992 [1966]: 529). No sustained 'spiritual conversion' towards class compromise and conciliation had occurred during this period. Institutions of class compromise in the Weimar Republic remained fragile. Support for class collaboration among the rank-and-file on both sides remained limited. The difficult economic situation severely curtailed the room for distributive compromises and ultimately contributed to the collapse of the Weimar Republic. Little over a decade after the signing of the Stinnes-Legien agreement important heavy industrialists decided to support Adolph Hitler in his bid for power (Hallgarten 1955; Turner 1985).

A sustained conversion of employers towards social compromise became possible only after World War II, when business resorted to the concept of the 'social market economy'. Even though, the Weimar Republic was initially characterized by cross-class collaboration, rather than conflict, employers and unions failed to construct a viable model of cross-class cooperation and corporatist forms of interest reconciliation during this period. Before the collapse of the Weimar Republic in the wake of the economic crisis that started in 1929, however, capital and labor, once more, managed to come to a compromise on a major political issue: the introduction of unemployment insurance in 1927. German employers had long opposed the introduction of unemployment insurance, before eventually accepting its introduction in 1927. The next chapter looks at why, despite intensifying class antagonisms, a compromise on that issue became possible.

5 Business and the Origins of Unemployment Insurance: Protecting Work Incentives

A people of strong force of will and progressive energy would not brand itself with the stigma of inferiority...by passing a law about the insurance of unemployment; i.e., the acceptance of a [social] cancer by the state (...) Let us stop with this greenhouse culture and acclimate our people to a rougher climate. (...) Let us not forget that a healthy and just struggle for the daily bread is indeed advantageous (Deutsche Arbeitgeberzeitung, No.44, October 10th, 1920, quoted in Führer 1990: 212-213, translated by TP)

The topic of unemployment insurance is pivotal to the debate about the role of employers in the formation of the welfare state. The cross class coalition thesis and political accommodation thesis make opposite claims about the preferences of employers with respect to unemployment insurance. In 1927 Germany introduced public unemployment insurance. Before the war, in the German Empire, employers fundamentally opposed any form of unemployment insurance. After the war, in the Weimar Republic, they decided to endorse the introduction of public unemployment insurance. How can we explain this turn of employers from opposing to endorsing unemployment insurance? What motivated employers to change their mind? ⁹²

Unemployment insurance is a crucial case for the cross-class coalition thesis, a programme that is seen by protagonists of this argument as essential for firms relying on a high-skill production strategy. The cross-class coalition approach interprets the establishment of unemployment insurance as the product of a political alliance between labor and important segments of capital. The main motivation for employers to support unemployment insurance is seen in the assumed positive effects of unemployment insurance on skill investments. Building on insights from the VoC school, this explanation stresses the importance of unemployment insurance for encouraging investments in firm and industry-specific skills. Earnings-related unemployment insurance benefits guarantee the worker that his investment in specific skills will not be devalued during times of unemployment and thus ‘reward the

⁹² This chapter draws in particular on the PhD thesis by the German historian Carl Christian Führer (Führer 1990), which concerns the introduction of unemployment insurance in Germany (1902-1927), as well as on the work by Anselm Faust (Faust 1986, 1987) and by Michael Wermel and Roswitha Urban (Wermel and Urban 1949).

worker for his or her specific skill investment even when the worker is out of work' (Estévez-Abe et al. 2001: 152). Unemployment insurance is thus understood as an incentive for workers to invest in specific skills. Building on this insight, protagonists of the cross class coalition thesis suggest that employers that are dependent on specific skills actively promoted the introduction of unemployment insurance, because workers' investments in specific skills were in their economic self-interest (Mares 2003a: Ch.2 ; Estévez-Abe et al. 2001: 180-181).

The *political accommodation* thesis suggests an alternative explanation assuming that employers' acceptance of unemployment insurance derived from political accommodation, rather than from genuine preferences. Relying on Esping-Andersen's concept of decommodification, this approach expects employers to oppose unemployment insurance. Esping-Andersen defines *decommodification* as a policy outcome characterized by the fact that 'a person can maintain a livelihood without reliance on the market' (Esping-Andersen 1990: 22). Compensation during periods of unemployment makes workers less vulnerable to the risk of unemployment. It raises the reservation wage and is therefore likely to undermine work incentives. It is for this reason that Esping-Andersen expects employers to oppose social policies (Esping-Andersen 1990: 22). Following this approach, one should expect employers to oppose unemployment insurance, because of its expected negative effects on work incentives and labor supply. If this argument is correct, employers' acceptance of unemployment insurance is most likely the result from a strategic accommodation to a changing political context, rather than an expression of genuine employer preferences rooted in their economic interests.

This chapter analyzes the introduction of unemployment insurance in Germany with the purpose of examining the ability of these two competing hypotheses to explain the positions that German employers took during the political processes that led to the introduction of public unemployment insurance in 1927. Did employers actively promote the introduction of unemployment insurance, as the cross-class coalition thesis predicts? Or, alternatively, did employers accept unemployment insurance for strategic reasons as the political accommodation thesis predicts? What role did skill investments and strategic considerations play in shaping employers' position towards unemployment insurance? Answering this question has a twofold purpose. First, it is likely to improve our understanding of the role of employers in welfare state development; and, second, it is likely to further our theoretical understanding of how employer associations form their social policy preferences.

The two arguments differ in their predictions because they rely on markedly different assumptions about what kind of rationale employers follow in forming their political

objectives. The cross class coalition thesis relies on an *economic* rationale, the political accommodation thesis on a *political* rationale. The economic rationale consists of the goal of improving economic efficiency and labor productivity. The political rationale consists of the goal of maintaining political influence by accommodating to an unfavorable political context. By examining the relative importance of economic and political rationales and objectives, this chapter thus also contributes to a better understanding of what shapes employers' political behavior.

The chapter is structured as follows: after elaborating the arguments on which the two alternative explanations are based in some more detail, the chapter provides a detailed historical narrative of how the introduction of unemployment insurance came about. The chapter discusses the attitude of German employers towards unemployment insurance in the context of the Wilhelmine Empire and the Weimar Republic, respectively, and shows that differences in political context between these two regimes have been instrumental in making employers change their mind (section I-III). Finally, the chapter discusses the validity of the two alternative explanations with regard to unemployment insurance in the light of the empirical evidence (section IV).

Business and unemployment insurance: Two alternative explanations

German business had adamantly opposed calls for unemployment insurance up to World War I (as shown in section I). After the war, the employer federation VDA came to reverse its position and decided to endorse plans for a public unemployment insurance (as shown in section III). The cross-class coalition thesis and the political accommodation thesis provide two alternative ways of explaining and understanding this reversal. These two approaches differ in the kind of motivations they assume to have led to this change. While the *cross-class coalition thesis* suggests that the new position came about as a result of changing preferences among employers, the *strategic accommodation* thesis suggests that the change was merely a strategic adjustment of employers to an inevitable political reality. This section revisits the key arguments in this theoretical controversy, which were already briefly outlined in the introductory chapter.

Central to the cross-class coalition thesis is the argument that employers played a crucial role in welfare state development by actively promoting the introduction of new social policies. Estévez-Abe et al., for instance, expect that employers will actively promote unemployment insurance, because unemployment insurance encourages workers to invest in

specific skills⁹³ and thus skill-based production strategies. These authors argue that ‘social protection often stems from the strength rather than the weakness of employers’ (Estévez-Abe et al. 2001: 181). In a similar way, Mares argues that ‘for large firms, considerations about the need to institutionalize guarantees to their workers that the investment in their skills would not be undermined during periods of unemployment were of paramount importance’ (Mares 2003a: 147). In this view, employers are expected to promote unemployment insurance, because “institutions of social protection help employers overcome market failures in skill formation” (Mares 2003a: 251). This argument suggests an explanation of employers’ endorsement of the 1927 unemployment insurance law that builds on the reliance of dominant groups within German industry on asset-specific skills. The political accommodation thesis, in contrast, suggests an understanding of employers’ endorsement of unemployment insurance as a strategic accommodation to a changed political context, a context where continued opposition would have turned employers into ineffectual bystanders.

These two alternative explanations link to the theoretical controversy about the nature of employers’ social policy objectives. This controversy builds on a distinction between ‘genuine’ and ‘strategic’ preferences. Both explanations build on this distinction. Political behavior may be motivated by so-called ‘first order’ or ‘genuine’ preferences. Preferences are considered to be ‘first order’, or ‘genuine’ or ‘real’ or ‘pre-strategic’, when they derive directly from the perceived self-interests of an actor. They are unaffected by considerations about what is politically feasible. Alternatively, political behavior may be motivated by so-called ‘lower order’ or ‘strategic’ preferences. These preferences result from actors’ accommodation with what they consider politically feasible in a given situation. To put it simply, strategic preferences represent a ‘lesser evil’ or second best option to an actor. The cross class coalition thesis emphasizes the first type of motivation, the strategic accommodation thesis the latter .

The interpretation of the 1927 unemployment insurance reform as the result of a change in genuine preferences among German industrialists has been articulated in its clearest and most sophisticated form in the work of Isabela Mares:

...the change in the preference of employers from a rejection of any system of compensation against the effects of unemployment to a support of a system of contributory unemployment insurance is not simply a change in the strategic preferences of employers (that results from the interaction with other social actors) or of employers' anticipation of a policy outcome that has a high probability of being successful, but a change in the ‘real’ or ‘pre-strategic’ preference of employers, that is in turn caused by changes in the balance of power among employers from ‘traditional’ industries (such as iron and steel) to more skill-intense industries

⁹³ Unemployment insurance is one of three policies identified by Estevez-Abe et al. as promoting skill investments, the other two being income protection through collective bargaining and employment protection.

that rely more heavily on exports (chemicals, machine tools, electricals) and by differences in the structure of the risk of unemployment faced by these industries (Mares 1996: 30).

Consistent with this interpretation of business endorsement of unemployment insurance as driven by first-order preferences, Mares also emphasizes that employer support had been crucial for the success of the reform. Without the change in employer preferences the introduction of unemployment insurance would have been far less likely to succeed. Therefore, employer preferences constitute an important cause of welfare state formation:

This change in the preference of employers and their final collaboration in the introduction of unemployment insurance is *the crucial factor* which facilitated the passing of the unemployment insurance bill in 1927 (Mares 1996: 5 , emphasis added by TP).

This chapter takes issue with this account and develops an alternative account which explains employers' endorsement of unemployment insurance as the result of a *strategic accommodation* by German business to changes in the political context. I argue that employers' genuine, first-order, preference had been a labor market free of any form of unemployment protection. Given that this option ceased to be politically viable for specific reasons, employers were compelled to choose their 'lesser evil' among several of the politically viable options. As the range of viable policy options changed over time, employers decided to accommodate and changed their positions in turn. Positions changed because external conditions limited the range of options available. Employers were fighting for their economic self-interests, but which policy they considered to meet their interests best depended on the specific political context and how it shaped the policy options available to choose from.

Clearly, political behavior is in reality always motivated by a combination of real and strategic preferences, rather than exclusively by the one or the other. Developing strategic preferences on a given policy issue only makes sense for a political actor as long as the actor also holds a genuine, first-order preference related to that policy issue. Without holding any genuine preferences, there is no need for forming strategic preferences. However, which of the two components of actor motivations we put emphasis on is not a moot or abstract issue but is of importance for how we understand and explain the origins of the welfare state. If business support for social policy had been the direct result of genuine, first-order preferences, then any explanation of the historical origins of the welfare state has to take into account the economic self-interests of firms as a constitutive cause of welfare state development. If, in contrast, business support had been motivated by strategic considerations, then the political circumstances that motivated this accommodation turn out as the crucial

factor facilitating the political compromises that have shaped the formation of the modern welfare state, rather than the economic interests of firms per se. The two explanations thus lead to different explanations about the causal forces of welfare state development.

5. I The Wilhelmine Empire: Employers against Unemployment Insurance

In line with what the de-commodification thesis predicts, German employers had originally been strongly opposed to any form of support for the unemployed (Centralverband Deutscher Industrieller 1913: 2). After the war, they had come to change their position and, after a period of wavering and internal undecidedness, had in the end, in 1926, decided to cooperate with government in the drafting of a bill establishing a public unemployment insurance. In 1892, Bueck, the influential executive director of the *Central Association of German Industrialists (CDI)* had called unemployment insurance a ‘monstrous project’ (quoted in Faust 1986: 170). Three years later (1895), he had declared that unemployment insurance was ‘decisively rejected’ by the CDI (quoted in Faust 1986: 171). This section first briefly presents the positions of the other major political actors before turning to the reasons for employers’ opposition to unemployment insurance during the Wilhelmine Empire (1871-1918).

The political debate

The issue of unemployment insurance first appeared on the political agenda during the 1890s. At that time, public support to unemployed workers was very limited and unemployed workers often relied on union-run funds instead. Responsibility for supporting unemployed persons rested with the municipalities, which were responsible for organizing public relief works. From about the turn of the century on, some municipalities started to provide subsidies to union-run unemployment insurance schemes in order to alleviate the financial burden on municipal relief programmes (Hennock 2007: 308-314). A few towns also started to organize their own municipal unemployment insurance schemes (Hennock 2007: 315). Most municipalities, however, were reluctant to establish their own unemployment support schemes and favored a nationwide unemployment insurance instead (Führer 1990: 116-118).

Concrete proposals for a nationwide unemployment insurance programme came first from the bourgeois social reformers. In 1894, the economist Georg Adler produced the first proposal for a public unemployment insurance scheme, organized on a mandatory basis and financed jointly by the state, employers and workers (Faust 1986: 151). This proposal, as well as similar proposals by other reform-minded academics, did however not find much political endorsement. Support for these proposals came chiefly from the municipalities, which hoped

for a mitigation of the cost burden on municipal relief works (Führer 1990: 114-116). The municipalities were however unable to find powerful allies at that time.

The social democratic labor movement was split on the issue of unemployment insurance. At SPD party congresses in 1893 and 1894 a majority of delegates voted against proposals for public unemployment insurance (Führer 1990: 52). The social democratic labor movement was wavering between two options: unemployment insurance organized by the state or unemployment insurance organized by the unions, the so-called 'Ghent system'. The social democratic labor unions had started to build up Ghent schemes from about the 1890s on. These schemes provided benefits to union members only. The unions' main motivation for building up Ghent schemes was to use these schemes to mobilize the working class and to bolster their financial strength during strikes. In 1891, 12.9 per cent of all union members were insured against unemployment by Ghent schemes, by 1905 the share had increased to 65.6 per cent and by 1913 to 81.3 per cent (Führer 1990: 55).

The social democratic labor unions rejected the social reformers' proposals for public unemployment insurance and demanded instead subsidies by the state and by employers for their own Ghent schemes. The motivation for this position was twofold: First, unions feared competition by a public unemployment insurance programme to crowd out their own Ghent programmes. Second, they did not trust the sincerity of government intentions. In the hands of the authoritarian political regime, they suspected, unemployment insurance would become a tool that would be turned against the working class. The unions suspected that the government would misuse unemployment insurance for wage dumping and the disciplining of the working class, in particular by forcing benefit recipients to accept low-paid or under-skilled jobs or to serve as strike breakers (Führer 1990: 59). Under the conditions of an authoritarian political regime, the labor unions were thus not prepared to entrust the state with supporting the unemployed.

Within the Social Democratic Party views diverged. The social democratic labor unions ("*Freie Gewerkschaften*") formed the moderate wing of the party and had a strong voice within the party. Consequently, a large part of the party supported the Ghent system and preferred public subsidies to these schemes, instead of a public programme. Supporters of a public unemployment insurance initially remained a minority within the party. Only in the years before World War I (ca. 1911-1914) both the party and the unions shifted their stance in favor of a position aiming at a public insurance solution. The Ghent system was now perceived as being only a transitional solution for the problem of unemployment, while in the

longer run unions and party would aim at a public unemployment insurance in tandem with a democratization of the political regime (Führer 1990: 67-69).

Industrial employers and unemployment insurance

The stance of industrial employers towards the issue of unemployment insurance was more stable during that period: they resolutely opposed any form of financial support to the unemployed. Their opposition was motivated by two basic types of concerns. First, they suspected that unemployment insurance would have negative effects on work discipline and work incentives. Second, they feared an unbearable increase in labor costs (Führer 1990: 201-221). Regarding the first concern, unemployment insurance was suspected to undermine the employer's position of authority vis-à-vis his workers, thereby corroding work discipline. Unlike programmes that protect against the risks of old age, disability, sickness and work injury; unemployment insurance protects workers that are in principle capable to work. Unemployment insurance makes individual workers less dependent on their employer by providing them with a prospect of maintaining a livelihood even without working. Programmes insuring against the risks of old age, disability, work injury and sickness protect only those types of workers that would be unable to work anyway or could not be expected to work. Unemployment insurance, in contrast, protects workers who are, in principle, assumed to be capable to work. Unemployment insurance reduces their dependence on work and thus the authority of the employer over them.

German employers at that time suspected that the decline of workers' dependence on work, their decommmodification, would harm work discipline and foster idleness. They suspected unemployment insurance to promote the formation of an 'army of layabouts', workers who would prefer to live from social benefits rather than work. Consistent with this view, employers also blamed unemployment on deficiencies of the individual. They understood the occurrence of unemployment as the result of an individual worker being unfit or unwilling to work, rather than as the result of macro-economic conditions. Employers argued that unemployment was generally low and, where unemployment occurred, it would usually be the fault of the unemployed person itself. Employer periodicals presented unemployment insurance as being a mere 'premium on laziness' financed by the employer (Der Arbeitgeber, No.2, 15.01.1914: 18) (also DAGZ, No.8, 23.2.1919: 2) (Faust 1986: 170-172). In short, employers opposed unemployment insurance because of suspected negative effects on work incentives.

The second reason why employers opposed unemployment insurance concerned the suspected rise in labor costs. Industry pointed out that it had already accepted the introduction of several social reforms in the 1880s, and was now unable to cope with any further increase in labor costs (Faust 1986: 170). Bismarck's social insurance reforms in the 1880s included programmes for the protection of workers against work injury, sickness, occupational disability and old age. These reforms were supported by German industry primarily because the reforms were seen as an instrument for the pacification of the working class (see chapter 3). The reforms, however, failed to have the expected pacifying effect and unions continued to gain strength during the 1890s and 1900s. The CDI noted this with discontent (Bueck 1905a: 792). Soon after Bismarck's social policy reforms had been enacted, German industry changed its position and turned against the further expansion of social insurance as intended by the government. German industrialists started to argue that the financial limits of social policy expansion had now been reached. Higher labor costs would harm industry's international competitiveness and lead to job losses (Büren 1934: 60-86).

The bourgeois parties seconded the employers' position. The Conservative Party, representing the interests of the landed aristocracy and agriculture, was resolutely opposed to unemployment insurance. Due to the massive migration of workers into the cities, agriculture was suffering from a lack of labor supply. The Conservatives suspected unemployment insurance to eliminate the incentives for unemployed urban workers to return back to agriculture and, for this reason, sided with the employers. Also the National Liberal Party, the party with the closest ties to industry (see tables 3.2), rejected proposals for a public unemployment insurance scheme, arguing that such plans would undermine the sense of personal responsibility among workers.

The Catholic Center Party, which had a very heterogeneous social base, remained internally divided and remained inactive on this issue. The two small left-wing liberal parties, *Freisinnige Partei* and *Deutsche Volkspartei*, were considering supporting a public unemployment insurance but remained, on the whole, inactive on this issue. To conclude, before World War I, German employers could rely on the support of a stable parliamentary majority against the introduction of public unemployment insurance. Last, but not least, the national government was reluctant to take up the issue and remained inactive, thereby implicitly supporting those opposed to public unemployment insurance (Führer 1990: 95-106 for the positions of the bourgeois parties and the government).

Employer arguments against unemployment insurance

The variety of specific arguments put forward by employer associations against unemployment insurance ranged from ostensibly technical arguments, e.g. claims that the lack of statistical data would make the calculation of the costs of the programme impossible, to arguments of principled opposition. What all arguments boiled down to was an uncompromising rejection of any form of support to the unemployed. This subsection elaborates in more detail the arguments frequently used by German employers against unemployment insurance in the Wilhelmine Empire.⁹⁴

No systematic unemployment. First and foremost, the political legitimacy of unemployment insurance was questioned. According to a memorandum by the CDI, there is no need for unemployment insurance, because there would be a sufficient supply of jobs anyway and thus everybody willing to work would find work. According to the report, unemployment would be an isolated phenomenon and, to the extent it actually exists, would be primarily the fault of the individual worker, due to the worker's idleness and lack of work discipline (Centralverband Deutscher Industrieller 1913: 3 and 15).

Regional imbalances. The same report suggested that unemployment would primarily reflect regional imbalances in labor supply, in particular due to the widespread rural exodus, which had led to a lack of labor in agriculture and an oversupply of labor in the cities (Centralverband Deutscher Industrieller 1913: 4). It was feared that the introduction of public unemployment insurance would encourage the rural exodus even further, as the problems of not being able to find a job in the city would be alleviated by the new insurance programme.

Rewarding idleness. The argument that unemployment would in practice not affect the hard-working and skilled among the workforce and that unemployment insurance would thus benefit only the 'undeserving' is a recurring theme in the statements of business representatives at that time. Unemployment insurance would only benefit those kinds of workers that were lazy, unskillful, incapable, rebellious or tried to dodge work. In 1913, Fritz Tänzler, the executive director of VDA, pointed out that unemployment insurance would mean that the hard-working ("Tüchtigen") would need to subsidize those that were idle and unqualified ("Mindertüchtigen") (quoted in Führer 1990: 84-85). Moreover, the problem of unemployment was seen as being artificially 'talked up' by the Social Democrats and the unions, who would intend to stir up social unrest (Führer 1990: 84).

⁹⁴ For the analysis of employer statements towards unemployment insurance during the pre-World War I era I rely to a large extent on Führer, a German historian who wrote his PhD thesis on the 1927 unemployment insurance reform (Führer 1990: in particular 82-93). All quotes translated into English by TP.

Weakening the sense of personal responsibility. Congruent with this view, employers also repeatedly voiced the concern that a public unemployment insurance programme would undermine the sense of personal responsibility among the workers. The following statement from a conference of employer-run labor exchanges (1903) reflects this view:

First of all, unemployment is not an evil, to the contrary, most people see work as an evil and unemployment as the desirable state, and if one is reasonably protected from the material setbacks that use to come along with unemployment, the larger part of the population will seek to enjoy the blessings of the new insurance (quoted in Führer 1990: 86, translated from German by TP).

Undermining work effort and work discipline. If the prospect of unemployment ceases to constitute a threat to the worker, the employer loses an important disciplining device: the dismissal. The worker will be less willing to make a serious work effort, if the prospect of unemployment becomes less frightening. The following statement made at the same employer conference in 1903 mentioned above, illustrates this concern:

The means for maintaining [work] discipline, which the employer has to his discretion..., are reduced to a minimum, or are removed completely. The only right, that remains to the employer, although with qualifications and conditions, is that he may dismiss the worker, and that the worker than is exposed, at least for a certain period of time, to the danger of unemployment. To avoid this danger, the workforce will, after all, still undertake some effort (quoted in Führer 1990: 87, translated from German by TP).

Raising the reservation wage. Another argument used against unemployment insurance was the suspected harmful effects on wage flexibility by raising the reservation wage. Alexander Tille, a representative of the German heavy industry, declared in 1908 that a public unemployment insurance would prevent unemployment from pushing down wages during times of economic crisis, thereby erasing the market mechanisms of demand and supply (Führer 1990: 86-87). As with the introduction of unemployment insurance, workers would stop to face a massive loss of income as a result of economic crisis, they would also become more reluctant to accept wage reductions during periods of economic crisis.

Undermining entrepreneurial authority. Closely related to the arguments concerning work effort and work discipline were arguments concerning the employer's authority over his workforce. As the quotes above show social psychological reasoning was applied to show that unemployment insurance would have hazardous effects on the workforce. Unemployment insurance was suspected to weaken the employer's authority in the workplace. Tille, for instance, argued that:

In every such [economic] crisis [the worker becomes aware that only the entrepreneur is capable to create jobs]. This way, he [the worker] learns to look up to the entrepreneur,

because he senses that his economic well-being is in his hands. He will, voluntarily, call him master (quoted in Führer 1990: 88, translated from German by TP).

Opposition by German business to unemployment insurance before World War I appears to have been unanimous. All segments of business shared the same reservations against unemployment insurance. Not only the large industrialists in the heavy industry, with their authoritarian ‘master in my own house’ approach, but also employers in the manufacturing industries, agrarian employers and small businesses were opposed to unemployment insurance. There appears to have been no sectoral cleavage on unemployment insurance (Faust 1986: 175-177; Führer 1990: 90-93; Ullmann 1976: 153-154).

German employers viewed the union-run Ghent schemes with even greater suspicion than public unemployment insurance. These schemes provided benefits to organized workers only and were used by unions to mobilize workers and to strengthen their financial resilience during industrial conflicts. Employers called on the state and the municipalities not to subsidize Ghent schemes as these schemes were used by the unions as a means to sustain strike action. The CDI declared in 1911 that by giving tax-financed subsidies to Ghent schemes, employers would be coerced to ‘sharpen the knife that is going to be turned against them’ (quoted in Führer 1990: 89, translated by TP). In the same way, also the peak-level employer federation, the VDA, opposed any public subsidies to Ghent schemes. In Bavaria, where some municipalities subsidized Ghent schemes, the Association of Bavarian Metal Industrialists threatened in 1909 to relocate plants away from municipalities that supported local Ghent schemes (Führer 1990: 89).

In short, the opposition of German employers to unemployment insurance in the pre-war period disconfirms the cross class coalition thesis, while it does provide evidence for the validity of the decommodification thesis. Arguments concerning skill formation appear not to have played a significant role in the political debate about unemployment insurance during that period. Even if they would have, such arguments would have been clearly at odds with the resolute opposition of German employers to the introduction of unemployment insurance. Instead, the arguments used show that German employers at that time were primarily concerned about the suspected hazardous effects of unemployment insurance on work discipline and work incentives. The opposition of German employers to unemployment insurance before World War I can be explained by the de-commodification thesis. Employers opposed unemployment insurance because they suspected an erosion of work discipline and work incentives.

German industrialists at that time did not see unemployment insurance as a means of encouraging investments in specific skills. They were not aware of the potential effects of unemployment insurance on skill investments. Unemployment insurance was suspected to promote idleness, reduce labor supply and harm work discipline, while at the same time increasing labor costs. Alexander Tille warned that with unemployment insurance, social welfare would lose the 'character of alms' and thus also its stigmatising character. A representative of the metal industry warned that unemployment insurance could lead to a situation where nobody would be prepared to work anymore (both statements quoted in Faust 1986: 172). In short, employers expected unemployment insurance to reduce, not to increase, the supply of capable and skilled labor. The initiative for protecting workers from the risk of unemployment came from the unions and their Ghent schemes, rather than from employers.

5. II The Introduction of Unemployment Insurance in the Weimar Republic

In the Weimar Republic, a political majority in favor of unemployment insurance emerged and made the introduction of unemployment insurance possible. In July 1927, the national parliament passed a law that introduced unemployment insurance. The new programme of unemployment insurance replaced the pre-existing programme of unemployment assistance, a means-tested programme administrated by the municipalities introduced in 1918. In addition, the law reformed the administration of labor market policies and put the national labor market authority and its job placement agencies under the control of tripartite bodies, consisting of employers, unions and the government. The administration of the new programme of unemployment insurance was entrusted to the newly created tripartite labor market authority. This created a close organizational link between the job placement services and the administration of unemployment insurance and, at the same time, involved employers and unions in the administration of both.

The law had the support of a broad parliamentary majority. The non-socialist governing parties and the opposition Social Democrats supported the bill. Only the communists, the Nazis and several deputies of the right-wing nationalist DNVP voted against. The bill was the result of a political compromise that the employer federation also decided to endorse. Only shortly after the passing of the bill, the deteriorating economic situation led employers to abandon this compromise and demand a return to means-testing. This section analyzes the political debates in the Weimar Republic that preceded the introduction of unemployment insurance as well as the positions of employers during these debates.

For the expansion of the welfare state, the Weimar Republic provided conditions that were favorable in political terms, but unfavorable in economic terms. Democratization for the first time gave the Social Democrats a chance for participation in national government. At the same time, economic development was characterized by high volatility and recurring economic slumps. Throughout the period of the Weimar Republic (1918-1933), real GDP per capita hardly ever reached the levels it had reached before the war (Schmidt 1998: 40). High levels of unemployment became a recurring phenomenon. After the war, demobilization led to a massive rise of unemployment caused by the difficulties of integrating the large number of soldiers returning from the front into a stagnating economy. The economic disruptions of the demobilization period were followed by a short inflationary boom during the period of 1920-1922, driven by a weak currency and the resulting boost to exports (Feldman 1984: 55-66). This had temporarily mitigated the problem of unemployment. With the onset of hyperinflation in 1923 and the currency reform unemployment began to rise again (Faust 1987: 264).

In November 1918, the new revolutionary government, led by the Social Democrats, had responded to the imminent problem of mass unemployment by establishing a programme of mandatory unemployment assistance (*“Erwerbslosenfürsorge”*). By way of an emergency decree, initially valid only for the period of demobilization, the government obliged municipalities to provide financial support to the unemployed. This programme was understood as a temporary solution, which was to be replaced with a permanent programme of unemployment insurance in due course (Führer 1990: 170; Büren 1934: 198). The programme provided means-tested flat-rate benefits to all non-employed persons who declared to be ‘willing to work’. The programme was financed by the municipalities, the regional states and the federal state. Municipalities had to administrate the programme and had substantial discretion in applying the rules of benefit eligibility (Wermel and Urban 1949: 21-23). As the municipalities were also in charge of social assistance they had little incentive to be restrictive with granting unemployment assistance benefits, as doing so would have merely shifted costs from one programme to another.

The programme of unemployment assistance became a crucial catalyst for making German employers change their mind regarding unemployment insurance. The introduction of unemployment assistance had changed the policy status quo against which employers had to evaluate the value of unemployment insurance. German employers were highly discontent with unemployment assistance and the way it was administrated. In their view, the municipalities were insufficiently checking need and willingness to work and were handing

out benefits in an indiscriminate way. The introduction of unemployment assistance had created a new reality for employers, one that they perceived as even worse than unemployment insurance. Before the war, the alternatives on the political agenda had been either unemployment insurance or no compensation to the unemployed at all. Now, the alternatives on the agenda were either unemployment *insurance* or unemployment *assistance*. The following subsection deals with the political debates about unemployment assistance and unemployment insurance from 1918 to 1927, before turning to the question why unemployment insurance had finally changed from being the ‘unspeakable evil’ to being a ‘lesser evil’ for German employers in section III.

The political debate

The initiative for the introduction of unemployment insurance after World War I came from the government. The introduction of unemployment assistance in November 1918 was intended as a temporary solution which would have to be replaced by a programme of unemployment insurance in due course. The government’s main motivation for promoting unemployment insurance was to alleviate the cost burden on the state by shifting some of the costs to the two sides of industry. Unemployment insurance would need to be financed by workers and employers through payroll taxes, while unemployment assistance was financed initially solely by general tax revenues. Already in August 1919, the Minister of Finance, Matthias Erzberger (Center Party), noted the ‘dismal experiences’ the government had made with unemployment assistance and declared the introduction of unemployment insurance ‘as soon as possible’ as a key priority for the government, in order to alleviate the burden on public finances (Führer 1990: 171). Four years later, in September 1923, Rudolf Hilferding, a social democratic Minister of Finance, called the introduction of unemployment insurance an ‘essential requirement’ to deal with the ‘catastrophic financial situation of the state’ (Führer 1990: 181). By shifting the compensation of the unemployed from the assistance to the insurance principle, the government intended to shift the financial burden to employers and employees.⁹⁵

⁹⁵ After the war, a significant expansion of social policies had occurred, resulting in substantial increases in social expenditures. At the end of the 1920s, social expenditures as a share of GDP were four times as high as before the war. During the same period, total payroll taxes had increased from 8 per cent to 15.5 per cent (Hentschel 1983: 129). This development had various causes: partly, this was the result of deliberate social policy expansion, partly due to economic stagnation and rising numbers of benefit claimants. Social policy expansion started already immediately after the end of the war. The introduction of entirely new programmes, such as unemployment assistance, and the extension of existing programmes to new social groups led to a substantial increase in public social expenditures. Compensating war victims was one key motivation of social

The introduction of unemployment insurance happened at a time of enormous instability, both in political and in economic terms. Economically, the period between 1918 and 1927 was characterized by high volatility in economic production and recurrent experiences of high inflation and mass unemployment. The unpredictable character of economic development at that time provided unfavorable circumstances for the establishment of a major new welfare state institution. Economic volatility made the number of persons that the new programme would need to support very difficult to predict.

Equally important, political instability contributed to the difficulties of introducing unemployment insurance. The Ministry of Labor had produced a first internal draft for an unemployment insurance law already in November 1919. It took all in all three government bills and several revisions until parliament would pass unemployment insurance in 1927. During the period of the reform process, from November 1919 to July 1927, Germany had experienced in total eleven different government cabinets. Most of them had to rely on weak parliamentary support, only three of them were backed by a parliamentary majority.⁹⁶ The first three coalitions, up to June 1920, were led by the Social Democrats; the majority of the following coalitions (5) were led by chancellors belonging to the catholic Center party.

The successful introduction of unemployment insurance during this period of political and economic instability was greatly facilitated by two factors: First, the commitment by the Minister of Labor and the ministerial bureaucracy to the project of unemployment insurance played an important role. Despite the frequent changes in government, the post of Minister of Labor was consistently held by the same person, *Heinrich Brauns*, throughout most of the period, from June 1920 to June 1928 (Preller 1949: 529-532; Faust 1987: 264). Brauns was a catholic priest and belonged to the Center Party. Brauns took the role of a policy entrepreneur in the reform process. He generally advocated a policy of compromise between capital and labor and actively promoted social policy expansion.⁹⁷ As the minister in charge he had been able to follow through the project of unemployment insurance nearly throughout the entire period. His role as a policy entrepreneur had thus played an important role to make the introduction of unemployment insurance possible (Führer 1990: 173-175) .

policy expansion. In 1920, social benefits for 1.5 million war disabled persons and 2.5 million war orphans and war widows were introduced. Another key motivation of expansionary reforms was to set off benefit losses that resulted from inflation. In various programmes, benefit values were repeatedly increased; for example, by the 1922 reform of the pension system (Schmidt 1998: 42).

⁹⁶ The three government coalitions enjoying a parliamentary majority were the Grand Coalition (August 1923 to November 1923) and two non-socialist coalition governments ("Bürgerblock")

⁹⁷ A biography of Heinrich Brauns is available on the webpage of the German Historical Museum <http://www.dhm.de/lemo/html/biografien/BraunsHeinrich/index.html> (accessed 03-01-2008)

Second, in spite of the frequent changes in government, a stable parliamentary majority in favor of unemployment insurance emerged nevertheless. While before the war, most parliamentary parties had either opposed unemployment insurance (National Liberals and conservative parties) or had been internally divided (Social Democrats and Center), now, in contrast, a majority of parties did in principle support unemployment insurance. The catholic Center party had overcome its pre-war disagreement and had become an advocate of unemployment insurance. The non-socialist parties were generally discontent with unemployment assistance, which they perceived as handing out generous benefits to layabouts and as being prone to benefit abuse, and saw unemployment insurance as an effective way of better controlling benefit entitlements (Führer 1990: 171).

Importantly, also the Social Democrats changed its position. The social democratic labor unions abandoned their pre-war demands for a state subsidized Ghent system and now supported a public insurance solution instead. The occurrence of mass unemployment during the first months of the war and during the demobilization period after the war had confronted the unions' Ghent schemes with massive financial problems, which had made the unions more skeptical about the advantages of the Ghent schemes (Wermel and Urban 1949: 24-25). At the same time, the democratization of the state had made labor's suspicions about the state abusing unemployment insurance as an anti-labor weapon redundant. Both aspects facilitated labor's shift to supporting public unemployment insurance. While the SPD and a majority of social democratic labor unions favored unemployment insurance, a minority within the labor movement remain opposed to the introduction of unemployment insurance and favored the continuation of unemployment assistance instead⁹⁸ (Führer 1990: 189-201). In December 1921, the majority of the unions organized in the Federation of Social Democratic Labor Unions (ADGB) voted against the assistance principle and in favor of the insurance principle (ADGB 1921: 19). A majority of social democratic unions had thus supported the introduction of a mandatory public unemployment insurance, financed by payroll taxes and administrated together with employers on a parity basis.

⁹⁸ Opposition to unemployment insurance came from the left-wing within the SPD, as well as from the Independent Social Democrats (USDP), the Communists (KPD), and from those unions within which these factions were dominating (Führer 1990: 190). In particular, the largest white-collar union, *AfA-Bund*, affiliated with the left-wing of the SPD, and the *German Metalworker Association*, the largest single union in Germany, did remain opposed to unemployment insurance (Führer 1990: 192). These groups preferred unemployment assistance instead of unemployment insurance for redistributive reasons. These groups considered the financing of support to the unemployed by general tax revenues as socially more just than the financing by insurance contributions. Unemployment insurance would oblige workers to pay for the consequences of unemployment by themselves. In contrast, assistance financing by general tax revenues was burdening also the rich and was therefore preferred (Führer 1990: 189-195).

A coalition between the Social Democrats, the Catholic Center Party and other smaller centrist parties in favor of unemployment thus emerged, which provided a stable parliamentary majority in favor of reform (see table 5.1 below). The parties that remained opposed to unemployment insurance were the right-wing nationalist *German National Peoples' Party* (DNVP), which represented, among other groups, also agricultural employers, the Nazis (NSDAP) and the Communists.

Table 5.1 Distribution of Parliamentary Seats in the Weimar Republic

ELECTION (MONTH/YEAR)	01/ 1919	06/ 1920	05/ 1924	12/ 1924	05/ 1928	09/ 1930	07/ 1932	11/ 1932	03/ 1933
Legislative period	National Assembl y	I.	II.	III.	IV.	V.	VI.	VII.	VIII.
<i>Seats total</i>	<i>423</i>	<i>459</i>	<i>472</i>	<i>493</i>	<i>491</i>	<i>575</i>	<i>608</i>	<i>584</i>	<i>647</i>
NSDAP	-	-	32 ²	14 ²	12	107	230	196	288
DNVP	44	71	95	103	73	41	37	52	52
DVP	19	65	45	51	45	29	7	11	2
Centre	91 ³	64	65	69	61	68	75	71	73
DDP	75	39	28	32	25	20	4	2	5
SPD	165	103	100	131	153	143	133	121	120
USPD	22	83	-	-	-	-	-	-	-
KPD	-	4	62	45	54	76	89	100	81
Others	7	30	45	48	68	91	33	31	26

Note: parties in **bold** voted in favor of the unemployment insurance law

²including seats of the nationalist "Völkische"

³joint list together with Bavarian People's Party

Legend: NSDAP: National Socialist German Workers' Party, DNVP: German National Peoples Party, DVP: German Peoples Party, DDP: German Democratic Party, Center: Zentrum, SPD: Social Democratic Party, USPD: Independent Social Democrats, KPD: Communist Party. Smaller Parties are aggregated.

Source: Preller 1949: 180 , data compared with Gonschior 2005 for errors

Table 5.2 Business representatives in the Reichstag (1928)

PARTIES	DEPUTIES AFFILIATED WITH INDUSTRY	DEPUTIES AFFILIATED WITH SECTORS OTHER THAN INDUSTRY	TOTAL OF PRO- BUSINESS DEPUTIES
German National People's Party (DNVP)	9	9	18
German People's Party (DVP)	15	8	23
Center Party (Catholic)	3	6	9
Democratic Party (DDP)	8	3	11
Bavarian People's Party	1	1	2
Economic Party	1	12	13
Total	37 (out of 491)	39 (out of 491)	76 (out of 491)

Source: Lewinsohn 1931 (93-94). Note: The total number of seats in the Reichstag was 491, pro-business deputies made thus up about 16 per cent (or 76 deputies) of the parliament.

5.III Changing Employer Positions in the Weimar Republic

During the Weimar Republic German employers abandoned their pre-war opposition to unemployment insurance and did, in principle, accept the need for a public unemployment insurance, as did the majority of parliamentary parties (VDA 1923: 35-36). The VDA cooperated in the drafting of the government bill and accepted the final outcome. This change in position was accompanied by internal disagreements and several changes of position between 1919 and 1927. We can identify broadly three periods that characterize the development of employer positions. Following the introduction of unemployment assistance in 1918, a majority of employer organizations initially supported a change to unemployment insurance (1918-1922). A minority of employer associations remained opposed to unemployment insurance during this period, in particular those associations representing smaller and medium-sized firms. After the introduction of a payroll tax for the financing of unemployment assistance, employers turned against unemployment insurance and called upon the government not to go ahead with the planned programme (1923/1924). During the final phase of the reform process, employers finally abandoned their resistance and decided to cooperate with the government in the drafting of the bill (1925/1926).⁹⁹ The employer federation VDA eventually endorsed the bill passed by parliament, although several deputies representing industry voted against the bill. This subsection analyzes the motivations for employers to abandon their pre-war opposition to unemployment insurance and to cooperate with the government in the drafting of the details of the new programme.

During the Weimar Republic German employers confronted a political context that was entirely different from the pre-war Empire. Before the war industry could rely on the authoritarian political regime as its firm ally. After the democratization of the political system, the participation of the Social Democrats in government had put this alliance into question. For the change in employers' position towards unemployment insurance, two aspects turned out as particularly important: (i) the introduction of means-tested unemployment assistance in 1918 and (ii) the new political majority in favor of unemployment insurance. In the view of employers, the new programme of unemployment assistance was fundamentally flawed and even worse than unemployment insurance (Tänzler 1929: 207-208). In addition, a political majority in favor of unemployment insurance had

⁹⁹ This periodisation relies on the work by Büren (Büren 1934: 208)and Führer (Führer 1990: 209)

emerged after the Social Democrats and the Center Party had made up their minds. Both parties had been undecided about unemployment insurance before the war.

If they wanted to get rid of the disliked unemployment assistance scheme, employers had two basic options: either, to try to dismantle unemployment assistance entirely or, alternatively, to try to replace it with unemployment insurance. As the first option appeared politically much more difficult to achieve they eventually embarked on the second option as their 'second-best choice'. The change in political context had turned unemployment insurance turned into a "lesser evil" option for employers. The following subsections analyze the reasons why employers considered unemployment *insurance* as less problematic than unemployment *assistance*.

Employers' broader social policy objectives in the Weimar Republic

To understand industry's position towards unemployment insurance it is helpful to consider the general of industry towards social policies during the Weimar Republic. The paramount social policy objective of German industry during that period had been to contain social policy expansion and the increase in public social expenditure. During the early post-war period (1918/1919) business had been in a politically weakened position, due to the revolutionary threat and its dependence on the willingness of organized labor to cooperate. With the stabilization of the political situation employers became politically more self-confident again and started to become more outspoken and assertive in their social policy positions. Working time regulations had been their main target. With their attack on the eight-hour working day, a part of the Stinnes-Legien agreement, employers resumed their fight against state intervention and eventually brought about the collapse of cross-class cooperation in the ZAG. Their objections against the works councils law in 1920 is another case in point (see chapter 4).

More generally, employers demanded a reorientation of social policy towards a so-called productivity-oriented policy approach. Social policy should aim primarily at promoting economic production rather than at helping those in need (Tänzler 1923: 274). The main objective of social policy should be to support everything 'that promotes production and increases [product] demand' (Tänzler 1924: 2). By this, employers did not mean a form of Keynesian demand management, but primarily the containment of public social expenditure. From 1924 on, employers intensified their demands for cost containment and more cost effectiveness in social policy, after the social policy expansion of the previous years led to substantial increases in social expenditures (Tänzler 1929: 216). They denounced the 'surplus production of social policy legislation,' a depreciative phrase used by the VDA executive

director Fritz Tänzler (Tänzler 1929: 210) . The employer federation argued that social expenditure had reached the limit of what German firms could cope with and, thus, social policy expansion had to stop (VDA 1925a: 91). In a similar way, the other peak-level federations, the German Diet of Industry and Commerce (DIHT) and the Federation of German Industry (RDI) also complained that wages and payroll taxes had become unacceptably high and would, as a result, make firms unprofitable (Führer 1990: 204-205).

At the same time, German employers did not in principle challenge the political legitimacy and necessity of social policy. The VDA and with it a majority of employer organizations did not aim at dismantling existing social policies, but instead at the preservation of the status quo of social policy and the containment of future social policy expansion. Only a minority of business groups demanded a dismantling of existing social policy programmes. Employers were well aware of the political dangers that a radical dismantling of social policy might create. A dismantling of core social policy programmes was suspected to promote social unrest and a strengthening of militant forces within the labor movement. In 1922, Carl Duisberg, founder of the chemicals company *I.G. Farben* and president of the industry federation RDI between 1925 and 1930, had reminded German industrialists about the importance of containing the communist threat:

In foreign policy, as in social policy, we have...always been 'too late'. We have always realized the situation too late, have done the right thing too late, which naturally, because it was too late, remained without effect. We cannot afford another 'too late'. We always have to remain aware that bolshevist Russia stands in the east. There, there is only one will, one goal, to establish the dictatorship of the proletariat all over Europe (Duisberg 1923: 68, translated from German by TP)

German employers were trying to strike a balance between on the one hand avoiding a further increase in social expenditures, while on the other hand preventing a return of revolutionary dangers by making radical demands that would threaten political stability and class compromise. Duisberg's statement demonstrates the acute sensitivities among German employers about the looming dangers of failing to solve 'the social question'. In a similar way, the president of the VDA, Ernst von Borsig, warned about the political consequences of a complete dismantling of social policy institutions, stressing that this could lead to 'open or latent revolution' (Führer 1990: 207). The basic necessity of social policy remained thus undisputed among dominant industry groups.

Unemployment insurance vs. unemployment assistance

The main reason why employers preferred unemployment insurance to unemployment assistance concerned the issue of work incentives. The kind of arguments used against

unemployment *assistance* after 1918 were largely identical to those used against unemployment *insurance* before the war. Unemployment assistance would benefit only the layabouts and erode workers' willingness to work. Earnings-related unemployment insurance suddenly appeared as the lesser of two evils, compared to the means-tested unemployment assistance. Unemployment assistance, like social assistance, was suspected of promoting idleness and destroying the sense of self-reliance among workers.

This suspicion was furthered by the fact that municipalities tended to grant unemployment assistance benefits in an indiscriminate way to all non-employed persons that declared to be willing to work. No record of previous employment was required. Though recipients were obliged to accept work if offered, in a period of high unemployment a person's willingness to work was in practice often difficult to prove. In addition, employers resented the fact of not having any influence over decisions about the granting of benefit entitlements. Municipalities had little incentive to check benefit eligibility carefully, as they were also in charge of social assistance. Careful checking would have merely shifted costs from one programme to another. In short, employers opposed unemployment assistance because it had a strong decommodifying effect on the working class.

Inspired by social Darwinist thinking, German employers thought that means-tested assistance programmes would unduly promote the 'survival of the unfittest'. If there would be no social assistance, they reasoned, there would be fewer 'unfit' in the first place. This is because social assistance benefits were suspected of damaging the individual's energy and capacity for self-reliance (*Eigenverantwortung*). The following statement by Ernst von Borsig, president of the VDA from 1924 to 1931, illustrates this argument:

It is possible that without the social assistance provided by the state perhaps 50,000 people will perish who manage to get by with the help of this assistance. But it is also possible, that, if this assistance would not exist, 4 to 5,000 other people would develop their capacities and energy in such a way that this would be - seen purely from an economic point of view- even more important (Borsig quoted in Führer 1990: 206, translated by TP).

The arguments against social protection used by industry in the Weimar Republic were thus highly similar to the arguments used before the war (see section I), though now these arguments were not directed against social policies in general, but against social assistance. While the payment of social benefits to those who were 'willing and capable to work' was accepted, employers distinguished carefully between 'deserving' and 'undeserving' claimants. Facing the existence of unemployment assistance, employers in general abandoned their pre-war opposition to unemployment insurance and began to see the later as an alternative to the perceived deleterious effects of unemployment assistance. The payment of unemployment

insurance benefits required a record of previous employment and was thus thought to be less prone to erode work incentives or to promote idleness. In a reversal of their pre-war position, employers now discovered the advantages of unemployment insurance.

In December 1920 the peak-level industry federation (RDI) declared that unemployment assistance 'is necessarily seen as alms [by the recipient] and, in the long run, undermines the self-confidence and sense of personal responsibility of the workforce' and for this reason should be replaced by a 'mandatory public insurance against unemployment as soon as possible.' Objections of a principled nature against unemployment insurance could no longer be accepted as being of critical importance (decision by the RDI executive board on December 16th, 1920, printed in RDI 1921). In a similar way, the Chambers of Commerce in the Ruhr area declared in a joint memorandum in October 1920 that unemployment assistance would be 'demoralizing, because it only allows the state to take care, while an insurance would encourage the wage-earner to practice self-help and would keep alive the idea of self-reliance in him' (Führer 1990: 210, translated by TP). These statements confirm the hypothesis that employers' new support for unemployment insurance reflected a lower-order preference, motivated by the assumption that an insurance programme has less detrimental effects on work incentives.

The importance of accommodation to political constraints is also confirmed by what is known about the RDI's internal deliberations. The decision to endorse unemployment insurance was prepared by the RDI social policy committee. In a meeting of this committee, its speaker, the plant director Hubert Hoff, had invoked two arguments in favor of unemployment insurance. First, there would only be two options available, unemployment insurance and unemployment assistance. The third option, a dismantling of unemployment assistance without any substitution would not be available, as such an option would not have 'any reasonable chance of success'. Second, unemployment insurance would be 'the lesser of the two evils' because 'if the system of unemployment assistance is continued, the employer has no influence on the use of the funds' (protocol of the RDI executive board meeting on December 16th, 1920, stated in Führer 1990: 211). With 16 votes in favor and 5 votes against, the RDI social policy committee decided to endorse the introduction of unemployment insurance. Subsequently, the RDI executive board ratified this decision with only one vote against (Führer 1990: 215). The internal deliberations of the RDI thus show clearly that the endorsement was motivated by a strategic accommodation to the political context.

Not all business interest groups agreed with the new position, though. Opposition to unemployment insurance came in particular from associations representing smaller and medium-sized manufacturing firms. The German Diet of Industry and Commerce (DIHT), the federation of the regional chambers of commerce, took the lead within the camp of the opponents. In October 1920, the DIHT declared to have ‘substantial fundamental objections’ to unemployment insurance (Führer 1990: 213). Opposition to unemployment insurance was, however, not limited to small firm sectors. Also parts of big industry remained opposed to unemployment insurance. The *Deutsche Arbeitgeberzeitung (DAGZ)*, one of the leading periodicals articulating the views of big industry, continued to agitate against unemployment insurance even in the Weimar Republic, using the same kind of arguments as before the war (see epitaph to this chapter). Although the employer federation eventually endorsed the government bill, several deputies affiliated with industry voted against the bill in the parliamentary vote (see below).

Strategic arguments also played a role among those that decided to continue to oppose unemployment insurance. The position taken by *Adolf Haeusser* illustrates this point. Haeusser was the one member of the RDI executive board that voted against unemployment insurance during the decisive meeting mentioned above. He represented the chemical industry and was chairperson of the firm *AG Farbenwerke*. Haeusser justified his support for unemployment assistance by arguing that it would be ‘an imperfect regulation, and precisely for this reason it will soon be dismantled. Whereas unemployment insurance, once introduced, cannot be dismantled anymore’ (protocol of the meeting by the RDI executive board on December 16th, 1920, quoted in Führer 1990: 215). Haeusser thought that industry should better await a change in the balance of political power in order to then take the opportunity to try to turn back the state of social policy to its pre-war status.¹⁰⁰ Unlike a majority of German industrialists, he considered the changes in the balance of political power to be of a temporary nature and, for this reason, clung to industry’s pre-war position of opposition to unemployment insurance.

Policymaking: Turnabouts and strategic accommodation

The shift in the position of German employers towards supporting unemployment insurance could potentially have led to a cross-class alliance, as a majority among the unions also favored unemployment insurance over unemployment assistance. Indeed, in a decision by the ZAG board in October 1921, unions and employers unanimously called upon the government

¹⁰⁰ The view by Haeusser was supported by some other employer groups, in particular the employer association of Hamburg-Altona and the Chamber of Commerce Bremen (Führer 1990: 217, Fn.170).

to substitute unemployment insurance for unemployment assistance (meeting of the ZAG executive board October 13th, 1921 VDA 1921). However, the employer federation, VDA, conducted an about-turn in autumn 1923 and called upon the government not to go ahead with the planned reform. The deteriorating economic situation had made employers skeptical about the financial sustainability of the planned unemployment insurance.

In 1923, the inflationary boom of the early post-war period turned into a slump with hyperinflation and the collapse of the currency. Unemployment soared rapidly. During the autumn of 1922, at the peak of the boom, the number of recipients of benefits from unemployment assistance had reached a low of about 17,000 recipients. At the end of 1923 the number of recipients of unemployment assistance benefits had gone up to 1.5 million¹⁰¹ (Preller 1949: 166-167). In 1925, the VDA estimated that the introduction of unemployment insurance would cause a cost increase of about 30 per cent, as compared to unemployment assistance (VDA 1925a: 61). In short, employers became increasingly worried about the cost burden of unemployment insurance and got cold feet.

To alleviate the pressure on public finances, the government introduced a payroll tax for the financing of unemployment assistance in October 1923. Two thirds of the costs of unemployment assistance were to be financed by workers and employers in equal shares, whereas the remaining third was to be financed by the municipalities and subsidies from the regional and federal state level (Preller 1949: 364). For this decision no parliamentary endorsement was required. In addition, in February 1924, a record of previous employment (3 months during the last 12 months) was introduced as a qualifying condition (Faust 1987: 265; Führer 1990: 181-182). The long-term unemployed became thereby excluded from receiving unemployment assistance benefits. In effect, these changes had turned unemployment assistance into a hybrid programme, combining elements of the insurance principle with elements of the assistance principle. With this reform the government had made great progress in alleviating the public budget of the burden of supporting the unemployed. As we have seen above, this was also the original motivation of government for promoting the introduction of unemployment insurance (Führer 1990: 181).

Although the shift of the cost burden from the state to the two sides of industry could be expected to have weakened employers' resistance to the introduction of unemployment insurance, for the time being employers did in fact maintain their opposition to unemployment

¹⁰¹ This dramatic deterioration was partly the result of the 'Ruhr occupation', the occupation of the Ruhr area by France and Belgium in response to Germany defaulting on its obligations to deliver war indemnities. As a result of the occupation, production in the Ruhr heavy industry collapsed.

insurance. The introduction of work record requirements is likely to have reduced the concerns of employers about the dangers of benefit abuse and the ‘subsidizing of work-shy shirkers’, which had previously motivated their opposition to unemployment assistance. As a result, the necessity of shifting to unemployment insurance probably appeared less salient to employers.

In 1925, the VDA conducted another about-turn. The employer federation decided to cooperate with government in the drafting of the unemployment insurance bill. At same time, the federation decided to maintain in public its opposing position “for the time being”. By cooperating in the drafting of the law, the VDA expected to be better able to ensure that its concerns would be taken into account by policy-makers (meeting of the VDA social policy committee on January 27th, 1925 VDA 1925b; cf. also Führer 1990: 218). The VDA succeeded in changing some regulations in its preferred way and in the end decided to endorse the bill that was passed by the national parliament in July 1927¹⁰² (Erdmann 1927: 347).

In the policy-making process the VDA’s focus had been primarily on two concerns: cost effectiveness and the way the new programme would be organized. First, employers wanted the new programme not to be more expensive than the old unemployment assistance programme. Benefit levels should be kept moderate. Second, employers attached great importance to the organization of programme administration. They wanted employers to be involved in the administration of the new programme, rather than an unilateral administration by the state, primarily in order to control the cost effective use of funds and to make sure benefit abuse would be controlled. Employers also supported a close integration of existing job placement services with the administration of unemployment insurance in order to allow for the strict implementation of the work obligation rule (Büren 1934: 208-209, re. both points).

¹⁰² The ‘Law concerning unemployment insurance and employment services’ passed in July 1927 consisted of two parts: The first part established the new unemployment insurance programme, while the second part reformed the organization of labor market policy by establishing a new public authority for this purpose, the new ‘National Office for Employment Services and Unemployment Insurance’. The placement of unemployed workers and the granting of unemployment insurance benefits had been united in one organization. The new authority was governed by tripartite decision-making bodies, including workers, employers and the state on a parity basis. The old programme of unemployment assistance had been administrated unilaterally by the municipalities, which now lost many of their earlier competencies. Unemployment insurance benefits were granted only to those who were ‘involuntarily unemployed’, were ‘willing and capable to work’ and had been employed for at least 26 weeks during the last 12 months. Benefit payment was limited to a duration of 26 weeks. Benefit levels were earnings-related and means-testing was abolished (Faust 1987: 276; Führer 1990: 189). Compared to unemployment assistance, the new law thus improved the control of employers over the use of funds and the granting of benefits and at the same time reduced decommodifying character of social policy, by linking benefits to previous employment.

On some specific policy details, unions and employers managed to find common ground in the policy-making process. Both sides of industry wanted parity-based administration ('social self-government'), rather than direct administration by the state. Both sides wanted close organizational links between labor exchanges and unemployment insurance administration (Führer 1990: 255-256). Both sides demanded the state to continue to play a role in the financing of unemployment compensation in the form of public subsidies in order to keep the payroll tax low (Führer 1990: 292-293). Moreover, both sides also opposed occupational risk differentiation by way of differentiating the contribution rate across sectors (Führer 1990: 316-317). In short, in the deliberations over specific issues of policy design in the later stages of the decision-making process, employers and unions did often agree. Once employers had decided to support the project, possible disagreements between capital and labor about policy details were not a reason for delaying the reform. The convergence of employer and union positions about policy details should not, however, be mistaken for the occurrence of a cross-class alliance in favor of the introduction of unemployment insurance.

The decision by employers to cooperate in the drafting of the unemployment insurance was motivated by the goal of overcoming unemployment assistance as well as strategic considerations. In order to avoid becoming an irrelevant bystander to a reform project that enjoyed broad political support, the VDA decided to offer their cooperation. Only in this way could the VDA expect that its concerns about the organization and financing of the new programme would be taken into account. Unlike in the Wilhelmine Empire, a clear parliamentary majority in favor of unemployment insurance now existed.¹⁰³ As a result, employers now perceived to stand a greater chance of influencing the project if they relied on cooperation, instead of on opposition. One representative of the metalworking industry pointed out that it would be "completely useless...to take the stance: We do not want to have any unemployment insurance!" (Oppenheimer from the Association of Berlin Metal Industrialists, quoted in Jastrow et al. 1925: 113). A strategy of fundamental opposition would

¹⁰³ The parties of the various non-socialist coalition governments in power since November 1923 and the opposition Social Democrats all endorsed the introduction of unemployment insurance. In the parliamentary vote on July 7th, 1927, 335 deputies voted in favour and 47 voted against the bill. The votes against came from the Communists, the nationalist DNVP (German National Peoples Party) and the Nazis (Faust 1987: 276; Führer 1990: 189).

in the long run stand “no reasonable chance” to succeed¹⁰⁴ (meeting of the VDA social policy committee, January 27th, 1925 VDA 1925b).

While the employer federation (VDA) had officially endorsed the bill, several parliamentary deputies representing business interests voted against the bill or abstained from the vote. Most of them belonged to the right-wing nationalist DNVP. Most of these votes came from agricultural employers,¹⁰⁵ who did not want to participate in the unemployment insurance scheme because most agricultural workers would not have qualified for benefits. Some of the votes against the law however also came from big industry, for example from the coalmine director Bernhard Leopold. Among those industry deputies abstaining from the vote was the executive director of the Association of German Iron and Steel Industrialists (VDESI), Jacob Reichert, (Führer 1990: 220-221; Liesebach 1957: 116). Politically right-wing but of diverse sectoral backgrounds, these employers did not support the compromise endorsed by the VDA. Given the overwhelming majority in favor of the law, these business deputies however refrained from fighting their case. As we will see in the following subsection, the passing of the law had not been the end of the debate. Less than two years after the passing of the law, the onset of the economic depression led employers revitalize their campaigning against unemployment insurance.

In short, the support of employers for unemployment insurance was the result of an accommodation to a changed political context, rather than a reflection of underlying genuine preferences for the social protection of unemployed workers. Before the war, employers had adamantly opposed unemployment insurance. Once the programme of unemployment assistance had been introduced the range of policy options that were politically viable had become narrower. No policy of unemployment protection at all ceased to be a viable policy option. The choice now was not between either having some kind of public unemployment compensation or having none, as before the war, but instead between two different types of unemployment compensation: between unemployment *assistance* and unemployment *insurance*. Earnings-related unemployment insurance maintained a greater dependence of workers on gainful employment compared to means-tested unemployment assistance. Moreover, many municipalities tended to hand out unemployment assistance benefits in an indiscriminate way and often made little effort to enforce work obligation rules, as they had

¹⁰⁴ Even the German Diet of Industry and Commerce (DIHT) decided in November 1926 that steadfast opposition to unemployment insurance would be pointless. The DIHT had previously been adamantly opposed to unemployment insurance and was the last of the peak-level federations to fall in line with the new strategy of pragmatic cooperation.

¹⁰⁵ Out of the 6 DNVP deputies that voted against the law, 4 were agricultural employers (Führer 1990: 220, Fn207).

no incentive to reduce the number of benefit recipients. Employers decided to accept unemployment insurance because they considered it a lesser evil.

Reform of the new unemployment insurance system

The political compromise in favor of unemployment insurance turned out as very short-lived. Soon after the passing of the law, unemployment started to soar as a result of the onset of the depression in 1929. The number of unemployed persons¹⁰⁶ increased from about 1.2 million in June 1927 to about 6.1 million in March 1932¹⁰⁷ (Preller 1949: 166-167). The contribution rate (3%) had initially been set in a way that the programme would be capable to support up to 800,000 unemployed persons (Faust 1987: 276). The number of unemployed persons had soon started to exceed the maximum the programme was designed for. The level of future unemployment had thus been grossly underestimated by policy-makers. The law obliged the federal state to cover revenue shortfalls by providing loans to the insurance administration. This meant an ever-growing burden on the federal budget.

The massive deterioration in the finances of unemployment insurance led to a heated controversy over the issue of how to reform unemployment insurance. Employers revoked the 1927 compromise and demanded massive cutbacks to contain the increase in social expenditures. The positions among the political actors of how to reform unemployment insurance differed greatly and developed into what was perceived by the social democratic labor movement as a conflict over the principles of the German welfare state. Labor unions and SPD insisted on increases in the contribution rates, while employers and the DVP (German Peoples Party) demanded substantial cost cuts to solve the fiscal deficits.

At the center of employers' demands for cutbacks were two demands. First, seasonal unemployment should be excluded from unemployment insurance benefits¹⁰⁸ and second, means-testing of unemployment insurance benefits should be re-introduced (Büren 1934: 211-212). Employers thus abandoned the insurance principle and demanded a return to the assistance principle.¹⁰⁹ In 1930, the executive director of the RDI, Kastl, complained that unemployment insurance would 'eliminate the mechanisms of demand and supply on the

¹⁰⁶ Number of persons seeking work as registered at the labor exchange offices, Preller 1949 relies on official data from the national labor market authority (Reichsanstalt).

¹⁰⁷ Schmidt states that the later number was equivalent to an unemployment rate of about 30 per cent (Schmidt 1998: 47). To compare with, the number of unemployed persons receiving unemployment insurance benefits had been about 1.5 million in March 1932 (Preller 1949: 166-167).

¹⁰⁸ Seasonal unemployment occurred especially in agriculture and in construction. See Preller 1949: 365

¹⁰⁹ It was in particular the latter demand that was interpreted by the social democratic labor movement as an all-out assault on the institution of unemployment insurance as such (Timm 1952).

labor market’ and for this reason it would have become impossible to ‘adjust wages in line with business-cycle developments’ (quoted in Weisbrod 1978: 210). The short-lived nature of employers’ endorsement of unemployment insurance underlines the strategic nature of this endorsement. Employers’ endorsement of the insurance principle in 1927 did not reflect a genuine or first-order preference in favor of unemployment insurance, but an accommodation to an unfavorable political context.

5.IV What Motivated Industry to Change its Position on Unemployment Insurance?

Before World War I, German employers had unanimously opposed unemployment insurance as hazardous to work discipline and work incentives. In the Weimar Republic employers had by and large come to accept unemployment insurance. Why did this shift occur and by what concerns was it motivated? This section summarizes the reasons why German employers reversed their position from opposing to supporting unemployment insurance and discusses the relevance of strategic and genuine preferences in motivating the political decisions of German employers.

The decision of employers to finally endorse unemployment insurance was a response to a set of profound changes in the political context that had happened after the war. The analysis in this chapter has highlighted two specific changes: First, the introduction of unemployment assistance in 1918 and second, the emergence of a stable political majority in favor of unemployment insurance. The introduction of unemployment assistance in 1918 had established an institutional policy legacy that in interaction with the political majority in favor of unemployment insurance made a return to the pre-war status characterized by the absence of a public policy for the compensation of the unemployed politically very unlikely.

As we have seen in the preceding sections, the interest of employers in the issue of unemployment protection derived from the decommodifying effects of unemployment benefits. Unemployment benefits provide workers with some chance of making a living without gainful employment and thus reduce their dependence on their employer, as Esping-Andersen has pointed out (1990: 22). It is for this reason that employers have been so reluctant to accept the provision of social benefits to the unemployed. Protecting workers against the risk of unemployment was suspected to reward the ‘work-shy shirkers’ (“arbeitsscheue Drückeberger”) within the working class. Once workers would be able to get by without working, a good deal of them would tend to become unwilling to accept any work at all. Protecting workers against the risk of unemployment was acceptable to employers only under the condition that a way would be found to limit the payment of unemployment benefits

to those workers that were truly ‘involuntarily unemployed’ and truly ‘willing and capable to work’. Employers considered great care to be necessary to make sure that those unemployed workers not fulfilling these criteria, the ‘shirkers’, would not enjoy any benefit entitlements.

In this respect, unemployment insurance is less problematic for employers than unemployment assistance. The reason for this is that these two programmes differ in the extent they enable the unemployed population to make a living without employment. The work obligation of benefit recipients can be enforced more effectively in an insurance scheme compared to an assistance scheme. Unemployment assistance required no record of previous employment. In some instances, the level of the flat-rate benefits tended to approach wage levels, which eliminated work incentives for benefit recipients (Preller 1949: 365). The problem of controlling who is to receive benefits was exacerbated by the way the programme was administered. The municipalities were in charge of administering the programme unilaterally. They were seen by employers as not carefully enforcing the work obligation rule, which was supposed to limit benefits to those willing to work. In practice, the municipalities had little incentive to enforce the rule of work obligation, as denying the payment of unemployment assistance benefits would have merely shifted the cost burden to the municipal poor relief programmes. The administration of unemployment assistance thus denied employers any influence over the granting of benefit payments.

Unemployment insurance, in contrast, links benefit entitlements to the record of previous employment and thus limits the possibilities for workers to make a living without any gainful employment. In addition, unemployment insurance would be administered with the involvement of employer representatives, instead of by the municipalities, and would thus provide employers with some control over who should receive benefits. In short, unemployment insurance was less of an evil than unemployment assistance to employers, because it is better suited to maintain the benefit recipients’ dependence on gainful employment. Framed in terms of the need to maintain ‘the sense of personal responsibility’ and self-reliance among the workers, employers aimed at maintaining the work discipline and work incentives of the working class. Decommodifying the unemployed was a threat to this aim. Before the war, when no public policy for the protection against unemployment had been in place, employers’ objective had been to preserve the policy status quo. After the war, when the introduction of unemployment assistance de-commodified the working class even more than what unemployment insurance would do, the employers’ objective had become to dismantle unemployment assistance.

The second component in the explanation of the change in employers' attitude towards unemployment insurance was the shift in the political center of gravity in the Weimar Republic, compared to the Empire. The authoritarian government of the Wilhelmine Empire had been reluctant to engage with the issue of unemployment insurance, while a majority of parliamentary parties had either opposed unemployment insurance (National Liberals, Conservatives) or had been internally split (Zentrum, Social Democrats). After the war, the social democratic labor movement turned away from the Ghent system, which had come under enormous fiscal stress as a result of recurrent waves of mass unemployment. Instead, a majority of the social democratic labor unions and the SPD now endorsed a public solution to the problem of unemployment compensation. Also, the two major non-socialist parties, the German People's Party and the Center Party, were now endorsing the introduction of unemployment insurance. The balance of power had thus shifted against the preferences of employers.

Equally important was the fact that unemployment insurance had received a strong advocate in the form of the Christian-democratic Minister of Labor, Heinrich Brauns, who followed through the reform project from the beginning to the passing of the bill in July 1927. In short, given the strong political support in favor of unemployment insurance, employers realized that a full-fledged dismantling of unemployment assistance had little chances to succeed, though this is very likely to have remained their first-order preference. To avoid becoming irrelevant bystanders, employers decided to endorse unemployment insurance and cooperate in the drafting of the bill. Their intention for doing so was partly strategic, partly genuine. In terms of strategy, their intention was to improve their capacity to influence details of the new policy. In terms of genuine preferences, their goal was to prevent the continuation of the disliked unemployment assistance programme.

The strategic character of employer positions is confirmed by their recurrent reversals of position. After the introduction of unemployment assistance in November 1918 and the presentation of a first ministerial draft for unemployment insurance in November 1919, the two leading federations, the RDI and the VDA, had decided relatively quickly to endorse the introduction of unemployment insurance, albeit with some internal opposition. In autumn 1923, the federations changed their mind and called upon the government to stop the project. They now feared a further increase of public social expenditure by unemployment insurance due to soaring unemployment (Büren 1934: 201). The soaring of unemployment in 1923 had fuelled employers' concerns about the unpredictability of the cost impact of the new policy and so they developed doubts about the desirability of the policy change.

The opposition of employers to unemployment assistance alone were thus not sufficient to convince them of the advantages of the insurance option. Additionally, the insight that a strategy of radical opposition would mean to fight a losing battle was important for employers to finally decide to cooperate in the drafting of the new programme. However, the resulting political compromise remained a short-lived one. The economic depression that started in 1929 precipitated a massive financial crisis of the new insurance programme. Employers abandoned the compromise and began to attack unemployment insurance, advocating a return to means-testing and the hollowing out of the insurance principle (Büren 1934: 208-209). These reversals would have been unlikely if employers' support for unemployment insurance had been motivated by a genuine preference for protecting the unemployed.¹¹⁰

On a more general level, the acceptance of unemployment insurance by employers was facilitated by a changing understanding of the causes of unemployment. Before the war, employers argued that unemployment would be a phenomenon caused entirely by individual defects; such as laziness, lack of skill, or unruliness; and would not affect the good workers (see section II in this chapter). Given the occurrence of mass unemployment during the Weimar Republic this position had become incredible. Unemployment became now generally perceived as a structural phenomenon, caused not by deficiencies of the individual worker but by systemic conditions. Also German employers came to accept this new understanding. In their 1924 social policy programme, the VDA declared that unemployment was one of the 'most serious questions' of German politics at that time (VDA 1924). An article published in *Der Arbeitgeber*, the VDA's official organ, described unemployment as having 'the character of *force majeure*' (Wolff 1926). The understanding of unemployment as being caused by systemic conditions, rather than individual deficiencies, is likely to have contributed to employers' acceptance of unemployment insurance as politically legitimate.

There appears to be little evidence for the hypothesis that a concern for the protection of skill investments motivated employers to accept unemployment insurance. Arguments

¹¹⁰ Additional evidence for the strategic nature of employers' support for unemployment insurance is provided by the stress of employers that monetary support to the unemployed is only accepted by them as a 'policy of last resort' (Büren 1934: 202). Priority should be given instead to job placement services, vocational re-training, job creation programmes and public relief works. Only to the extent that such measures failed to reduce unemployment, should passive social benefits be granted (Büren 1934: 213). Employers by and large welcomed the use of public relief works, such as the programme of 'productive unemployment assistance' established in 1923, as a useful way of maintaining the unemployed persons' capacity to work¹¹⁰ (Büren 1934: 202; Preller 1949: 367). This general prioritisation of active measures over passive social benefits confirms the interpretation of employers' support for unemployment insurance as having been motivated not by a genuine preference but by strategic motivations instead. Employers accepted the payment of social benefits to the unemployed only as a second-best policy option, to be used only if measures to reduce unemployment failed.

relating to the protection of skill investments appear not to have played a central role in the debates leading to the introduction of unemployment insurance at all. Mares (2003), who stresses the importance of skill investments in making employers support unemployment insurance, provides only one specific piece of archival evidence relating to the protection of skills¹¹¹ (Mares 2003a: 147): ‘The condition of unemployment leads to the change in the profession of the unemployed, which is an extremely unfavorable situation for the training of workers in particular occupations and for employer who can hold on to their skilled workers only with great difficulty’ (VDA 1927: 136 , translation by Mares). We have to bear in mind that the degeneration of skills due to prolonged periods of unemployment that this statement refers to, takes place with or without the payment of unemployment insurance benefits. Concerns about skill degeneration may explain why employers demanded re-training activities, public relief works and improved job placement services, but not why they accepted social benefits to the unemployed. In short, arguments related to skill investments appear to have been of subordinate to the protection of work incentives and strategic considerations.

Table 5.3 Sectoral composition of German Industry (1927/28)

Sector	%
Mining	10.0
Stone and earth industry	4.1
Iron and Steel	10.3
Mechanical engineering and car manufacturing	8.2
Electric engineering	4.1
Chemical engineering	3.8
Textiles	7.6
Clothing	5.8
Paper and pulp	5.8
Leather	1.7

¹¹¹ I did not find any further business statements relating unemployment insurance to skill investments in the literature and sources consulted. For the analysis of business statements, I draw in particular on a PhD thesis on the genesis of the unemployment insurance law of 1927, written by the German historian Hans Christian Führer and the sources used there (Führer 1990). It is worth pointing out that this study barely mentions the issue of skill investments as a motivation of employers, despite the fact that the study also includes an in-depth analysis of the role of employers in the policy-making process (see, in particular 82-92 and 201-22).

Rubber	0.6
Timber industry	4.1
Food	14.7
Energy utilities	2.1
Construction	11.4

Note: Share of sector in percentage of total industrial output, sectors in **bold** are those relying on high-skilled labor.

Source: Weisbrod 1978: Table 1, p.34

Although direct archival evidence for the importance of preferences relating to the protection of skill investments is weak, it is still possible that underlying structural changes in the composition of German industry during the Weimar Republic have facilitated employers' policy reversal, as suggested by Mares (Mares 1996: 30). The newer manufacturing industries were more skill-intensive compared to the older heavy industry and for this reason may have been more open to labor demands. We therefore need to look at the relative importance of skill-intensive industries during the Weimar Republic. Following the definition of skill-intensive sectors used in Mares (chemicals, machine-tools and electric engineering) (1996: 30), only about 16 per cent of total industrial output came from these sectors at the time unemployment insurance was introduced in Germany (see table 5.3 above). Skill-intensive sectors did thus not dominate German industry at that time. It is therefore unlikely that concerns about the protection of skill investments had been the main factor explaining why employers decided to change their mind in the Weimar Republic.

To summarize, the argument presented in this chapter differs from a cross-class coalition argument in two important regards: First, the specification of the reasons for employers' reversal from opposing to supporting unemployment insurance and second, the relevance for the reform outcome that is attributed to this change. First, the chapter has shown that employers' acceptance of unemployment insurance reflected an accommodation to political constraints, rather than genuine preferences for social protection of the unemployed. Changes in politics and policy status quo motivated employers to change their positions on unemployment insurance. I argue that, before as well as after the war, the genuine preference of employers had been to limit the decommmodification of the unemployed as much as possible in order to maintain work discipline and work incentives. What the best way for employers was to achieve this preference changed over time due to changes in the policy status quo and

the balance of political power. Political accommodation can explain business support for social policies better than economic interests.

Second, the argument in this chapter differs from a cross-class coalition argument in respect to the causal impact that is attributed to employers for shaping the reform outcome. The existence of a cross class alliance presupposes that employers and unions cooperate with the purpose of jointly promoting a certain policy option, whether for strategic or for non-strategic reasons. The analysis of the reform process in this chapter does however not support the interpretation that the unemployment insurance law resulted from such a cross class alliance. Although the analysis did find that employers and unions found common ground on a number of important issues of policy design, the unstable and wavering character of employers' support for unemployment insurance did not allow the formation of a stable cross class alliance. The driving force behind the project had not been a cross class alliance but primarily the ministerial bureaucracy.

Remarkably, the reform took place at a time when class cooperation was crumbling. While during the early post-war period class cooperation was prevalent as a result of the Stinnes-Legien agreement and the ZAG, class cooperation eroded subsequently and the pre-war positions of class antagonism resurfaced (see chapter 4). Due to its strategic and narrowly conceived nature, the compromise over unemployment insurance was unable to revitalize class cooperation more broadly. The onset of the economic crisis in 1929 led to the collapse of class compromise and ultimately to the collapse of the Weimar Republic and the coming into power of the Nazis. Large parts of German industry had become disillusioned about the capacities of the parliamentary system to provide the necessary conditions for profitable production and turned to Nazism instead (Hallgarten 1955; Turner 1985). In short, a sustained and stable form of class cooperation or a cross-class alliance did not develop during the Weimar period.

Conclusions

This chapter has shown how the kind of unemployment policies demanded by industrial employers were shaped by the political context. In the German Empire, employers had been adamantly opposed to any form of public support to the unemployed. In the Weimar Republic, employers came to change their mind and eventually supported the introduction of unemployment insurance. The chapter has shown that this reversal reflected a calculated accommodation to far-reaching changes in the political context that would have rendered the continuation of fundamental opposition a losing battle. The chapter has emphasized, in

particular, two specific changes: First, changes in the balance of power between supporters and opponents of unemployment insurance. Before the war, a stable parliamentary majority against unemployment insurance existed: after the war, a stable parliamentary majority in favor of unemployment insurance emerged, because the Social Democrats and the Center Party, different to before the war, decided to support unemployment insurance. To avoid losing political influence by being bystanders to an unstoppable reform, employers decided to cooperate in the drafting of the government bill.

Second, before the war no public policy to support the unemployed had been in place. The work incentive mechanisms produced by the market forces had thus been fully operative. The programme of unemployment assistance introduced immediately after the war changed this. Unemployment assistance was a means-tested flat-rate benefit programme that could be paid to anybody out of work and gave employers no control over the granting of benefit entitlements. For this reason, employers strongly opposed unemployment assistance. Unemployment insurance, in contrast, based benefits on previous employment and earnings and gave employers some control over the use of funds through their participation in the administration of the new programme. As turning back the clock to the pre-war times was politically unfeasible, employers eventually decided to endorse the introduction of unemployment insurance as a lesser evil. By supporting the project they expected to be able to get rid of unemployment assistance and influence important details of the new policy, in particular its institutional infrastructure.

Both in the Empire and in the Weimar Republic the concern of employers regarding the issue of unemployment protection derived from the suspected work disincentives produced by the decommodifying effects of supporting the unemployed. The provision of social benefits to the unemployed reduces the dependence of the individual worker on gainful employment and for this reason was suspected by employers to erode work discipline and work incentives. It was not the protection of skill investments, but concerns about the erosion of the employer's control over the workforce that was the underlying pre-strategic preference that led employers to engage with the issue of unemployment protection. By supporting unemployment insurance employers tried to limit the decommodifying character of social policy, replacing a strongly decommodifying policy with a less decommodifying one.

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Employers' preference for Bismarckian social policies over universal and egalitarian alternatives was not limited to the issue of unemployment insurance but holds also for other

social policies. The conflict over Bismarckian vs. universalist social policies resurfaced again after World War II, when employers lobbied against a transformation of the German welfare state system towards a universalist system of so-called “unitary insurance”. This failure to transform the German welfare state is analyzed in chapter 7. Before that, chapter 6 provides a brief digression on how the political experiences made by German employers during the Weimar Republic and the Nazi regime influenced their broader attitudes toward social compromise and the importance of embedding profit-seeking activities of firms into the regulatory order of a “social market economy.”

6 German Business after World War II: Resort to the ‘Social Market Economy’

The change in the economic attitudes [Wirtschaftsgesinnung], in the economic forms and in the social order that has happened over the last 50 years, and that since 1948 continues in the Federal Republic, is expressed in the fact that nowadays we do no longer speak of a capitalist economic order but of a “Social Market Economy”. By this type of market economy one means an economy based on the principle of private ownership of the means of production, free competition within the framework of the legal order, freedom of contract, individual responsibility and a stable currency. This type of market economy is called social because its protagonists, which include the entrepreneurs, are committed to achieving the highest possible degree of social justice and security by using this order as the basis for the production and distribution of goods.

Quote from the declaration of principles by the German employer federation BDA ‘Gedanken zur Sozialen Ordnung’ (BDA 1953a: 5, emphasis in original)

The importance of the Nazi era and World War II as the catalysts of major transformations in German history is hard to overstate. The end of World War II turned out to be a critical juncture in the development of Germany’s political economy. During the late 1940s and the early 1950s the decisions were made that constructed or re-constructed those institutions of cooperation between capital and labor that are today seen as core elements of the German ‘coordinated market economy’. Coordinated wage bargaining and works councils were re-established following broadly the model of the Stinnes-Legien agreement. At the same time elements of state intervention in industrial relations were dismantled and co-determination at the firm level was introduced. Employers endorsed the political concept of a “social market economy” as an alternative to its leftist contenders, democratic socialism and communism. This chapter elaborates what this concept meant to employers and what motivated them to endorse the social market economy.

6. I The Social Market Economy as Ideological Weapon

Following World War II German employer associations reoriented their general approach to labor. They shifted from an approach of aggressive confrontation in the 19th century to accepting unions as an equal bargaining partner after 1945. The first attempts to establish a stable form of class cooperation had already been made after World War I through the ZAG committee established by the Stinnes-Legien agreement. Despite this attempt, the two sides of

industry did not, however, succeed in establishing a stable and sustained form of class cooperation during the Weimar Republic. Class antagonism and conflict eventually prevailed in a context of political and economic instability. Institutions for class conciliation remained disputed, in particular the role of the state arbitration boards. Economic crisis intensified distributive conflicts between capital and labor.

The political and economic developments after World War II, in the Federal Republic (FRG), stand in marked contrast to the Weimar Republic. The rapid rises of prosperity during the ‘economic miracle’ period went hand in hand with political stability, more stable forms of class cooperation and bargaining and the expansion of the welfare state. The receding of class antagonism after World War II and the development of more stable institutions of class compromise was accompanied by an ideational paradigm shift within the German business community. Employers became active protagonists of ‘social partnership’ and the so-called ‘social market economy’, as expressed by the BDA statement in the epigraph to this chapter (Bunn 1959: 379).

German business resorted to the ‘social market economy’ at a time when its political standing was weakened. The impression that financial support by the heavy industry had been important in helping the Nazis to come into power had weakened tremendously the political credibility of German industry (Hallgarten 1955; Turner 1985). Ludwig Rosenberg, the future president of the labor union federation (DGB) expressed this view:

It need only be repeated ...what Fritz Thyssen, the controller of *Vereinigte Edelstahlwerke*, reported in his book, *I Paid Hitler*. The world and the German people know what wretched and irresponsible roles he and numerous German industrialists played in those decisive months before Hitler came to power, and how the already bankrupt Nazi party was rescued through these politico-economic leaders. There is no doubt that without them the world would have been spared Hitler and the misfortune associated with him (Rosenberg 1953: 6 quoted in Bunn 1958: 283).

While nowadays the concept of ‘social market economy’ is often understood as a synonym for the welfare state, during the 1950s it represented well-nigh the opposite (Van Hook 2004: 291). Its protagonists understood the ‘social market economy’ not as an alternative to but as the implementation of economic liberalism. The social market economy represented a set of economic policy principles, championed by the Christian Democratic Minister of Economics, Ludwig Erhard, the chief political protagonist of the social market economy. Its defining goals were entrepreneurial freedom, free market competition and currency stability: ‘the social market economy celebrated the market, competition, and free trade’(Van Hook 2004: 3). Unlike other industrial societies that entered a period of greater

state intervention in the economy after World War II, Erhard's economic policies dismantled economic controls and turned to economic liberalism instead (Shonfield 1965: 240).

In German public discourse of the post-war period the concept of the 'social market economy' functioned as the political 'antidote' to 'democratic socialism' and communism. Democratic socialism was the political platform of social democracy in the post-war period. With the collapse of the Nazi regime, the hour of 'democratic socialism' appeared to have arrived. The British and the Americans considered the social democrats to be the representatives of a suppressed democratic tradition in Germany and initially supported social democratic plans for economic reorganization. With the onset of the cold war, the US turned away from economic reorganization, in order to enlist the economic power of Germany in the new east-west conflict. This meant the end to plans for a nationalization of the heavy industry (Van Hook 2004: 53-94).

German business and its political allies used the doctrine of the social market economy as an ideational tool to challenge competing doctrines of economic organization and demonstrate the superiority of a market-based order vis-à-vis its leftist alternatives. The political priority of German business was to resist the threat of 'democratic socialism', arguing that 'economic and social theory of democratic socialism fail' (BDA 1953a: 4). Moreover, the creation of a communist regime in the Eastern part of Germany (GDR) following the split of the German territory after World War II, made the danger of collectivization appear as even more real and serious. In this historical context, the 'social market economy' certainly appeared to German business not only as a lesser evil to be endorsed for strategic reasons, but also as the genuine savior of the capitalist order.

In 1953, the Federation of German Employer Associations (BDA) published a social policy manifesto titled '*Thoughts about the Social Order*' ["*Gedanken zur sozialen Ordnung*"] (BDA 1953a). This is the most important document published during the post-war period outlining the social policy doctrine of the federation and its understanding of the concept of 'social market economy'. The platform was presented shortly before the national elections in an apparent attempt to shape public opinion. The document is structured around a critical evaluation of three different ideological programmes: communism, democratic socialism and the social market economy - the latter being the one explicitly advocated by the BDA as an alternative to the other two. Democratic socialism and communism are presented as the main political rivals to the social market economy. In the 1950s, the social market

economy was not perceived as an alternative to a liberal market economy but instead as its materialization.

While the manifesto considers the flaws of communism as being obvious and does not spend much time on its refutation, ‘democratic socialism’ is considered as a much more serious programmatic contender. The document identifies collectivization of industry and centralized economic planning by the state as the defining characteristics of ‘democratic socialism’, referring to the founding congress of the Socialist International in Frankfurt 1951 (BDA 1953a: 3). The tenets of ‘democratic socialism’ were presented to be in conflict with individual economic freedom and, therefore, in violation of human dignity: ‘A social order based on human dignity is irreconcilable with its [democratic socialism’s] theories.’ (BDA 1953a: 4). Communism and democratic socialism were the programmatic contenders against which the doctrine of the social market economy was directed.

The doctrine of ‘social market economy’ was not a brainchild of German business, though. Instead, the concept was only adopted by business after World War II, while it has its intellectual roots among catholic social theorists of the Weimar period. The notion of a social market economy was first used during the 1920s by catholic academics at the University of Freiburg¹¹² (Bunn 1959: 370; Joerges and Rödl 2004: 12). After World War II, the concept became the overarching political doctrine of the Christian Democratic Party (CDU), which was the successor to the Center Party in the Weimar Republic. The Christian Democratic Minister of Economics, Ludwig Erhard, justified his free market policies by reference to this programme (Kreile 1978: 198-200; see also Nicholls 1994; and Van Hook 2004). The doctrine of the social market economy was the answer by business and the political right to the programme of nationalization and economic planning advocated by the left. The doctrine of ‘social market economy’ aimed at disarming these challenges by combining a political-economic order based on market competition with social peace and political stability.

In the view of German business the political struggle taking place in Germany at that time was between the protagonists of the social market economy, on the one hand, and the protagonists of collectivism on the other. That support by German business for the social market economy was intended as a weapon against socialism and communism is evident in the following summarizing statement taken from the 1953 Annual Report by the BDA:

‘Neither an anonymous collectivism, the power of organizations and functionaries, nor the socialization of the economy and the people, but the observance of the worth and freedom of

¹¹² The journal of the movement is *Ordo: Jahrbuch für die Ordnung von Wirtschaft und Gesellschaft*. To its group of contributors belong Friedrich A. Hayek, Alfred Müller-Armack and Wilhelm Röpke (e.g. Müller-Armack 1948).

individuals and the recognition and promotion of property rights and private ownership for all sectors of the society are the bases of our culture and of its appropriate social order. These bases alone can be the building stones for a spiritual dam against the dangers of bolshevist infiltration.

Not in systematic leveling, but only in individual initiative and responsibility can a social order be anchored which assures social well-being and progress.

Neither the communist state economy nor a socialist planned economy, but the social market economy has, as the facts and experiences in all countries show, actually demonstrated economic and social efficiency. To lead this social market system to even greater attainments remains the positive purpose and aim of the entrepreneurial economy. (BDA 1953b: 21,)

Remarkably, German business emphasized the *market* component, rather than the *social*, in the doctrine of social market economy. When German business referred to the concept of ‘social market economy’, the meaning of the adjective ‘social’ always remained very vague. First and foremost, the adjective ‘social’ stood for the general belief that a political-economic order based on free market competition would be a better means for achieving social ends than any alternative political-economic order:

We embrace the *social market economy* with its principle of private ownership of the means of production, with free competition within the framework of the legal order, with freedom of contract, with individual responsibility and a stable currency. Compared to the planned economy...., this type of economy guarantees a maximum of production of economic goods.... This type of market economy is the economic foundation for achieving the maximum of social justice, security and freedom for every citizen. This is the reason why we call this a “social market economy” (BDA 1953a, emphasis added).

From the view of German business, social ends had to be accomplished first of all by way of increasing economic production and national prosperity. Social policy should play only a secondary role. According to the protagonists of the social market economy, increases in economic prosperity for all should be achieved primarily through the market and not through the welfare state. The means to achieve this is wage policy, rather than social policy: ‘The goal of wage policy is....the participation of the worker in the expanding production; that is, an increase in his real wage’ (BDA 1953a: 6). The *social* of the social market economy was delivered by rising real wages, in line with the development of labor productivity, according to the view of the BDA.

The principle of social policy that the social market economy relies upon is *subsidiarity*. According to the doctrine of the social market economy, the welfare state should only have a subsidiary role, it should only step in when the market fails. This position relies on the argument that social justice can only be achieved if economic production expands and incomes rise. Social justice cannot be achieved by redistributing wealth through the welfare state but only by increasing economic output: ‘There is no sound social order that is not based on performance. One cannot borrow societal prosperity, one can only create it’ (BDA 1953a:

6). Increasing prosperity, in turn, is only possible on the basis of a free market economy. Yet, German business nevertheless accepted a role for public social policy in those areas where the market fails. Social protection would be necessary to maintain political stability and social peace:

The social conscience and the *raison d'état* require that the community steps in to help those citizens to secure their elementary preconditions of existence, who due to sickness, old-age, work incapacity, or other unavoidable fates, are not able to support themselves. This is a requirement of charity [Nächstenliebe]. Due to the natural imperfections of human beings...the requirement of charity...has to become law. (...) The limits are where the character and scope of public support threatens to paralyze the self-reliance of the citizen to care for himself and his family [Daseinskampf]. Public support must, therefore, remain subsidiary. Furthermore, it must not be extended into a universal 'insurance against all risks' [*Schicksalsversicherung*] (BDA 1953a: 6, emphasis in original)

This statement by the BDA documents clearly that German business did not support social insurance as a protection of skill investments, as suggested by the cross-class coalition thesis, but as a means to maintain social peace and political stability. In no part of the BDA social policy programme analyzed above is any link established between the requirements of skill formation and social policy. Instead, social insurance and the fight against unemployment are supported on the grounds of normative obligations ('social conscience') and political stability ('*raison d'état*').

The simultaneous emphasis on the subsidiary character of social policy and the importance of self-reliance also indicates the continued importance of work incentives for employers. The kind of social policies supported by employers were conservative social policies, social insurance schemes based on employment and with earnings-related benefits. This type of social policy maintains work incentives and does not liberate the individual from its principal necessity to work. As we will see in the following chapter (7.I) employers did fight for the maintenance of the Bismarckian welfare state institutions and against a system shift to a universalist model after World War II.

6.II Resort to Social Partnership

Parallel to the paradigm shift of German business to the 'social market economy' a shift in attitude towards the labor unions occurred. The old authoritarian and confrontational approach, known as the 'master-in-my-own-house' approach was first undermined by the Stinnes-Legien agreement in 1918. In the Weimar Republic institutions of social partnership remained fragile and contested, though, while more sustained and stable forms of social partnership developed only after World War II. This change was facilitated by a more profound paradigm shift among German employer associations towards social partnership and

social compromise following World War II. While the Stinnes-Legien agreement had been primarily strategic in nature, the turn to social partnership in the Federal Republic had a much more genuine and profound character. Nevertheless, the BDA drew on the Stinnes-Legien agreement to legitimate its turn to social partnership:

The social order is an essential component of our internal order [*innerstaatliche Gesamtordnung*]. Since the November Agreement of 1918 concerning the *Zentralarbeitsgemeinschaft* [Stinnes-Legien agreement], which leading and politically responsible representatives of the peak associations of employers and employees concluded, our German social order rests on the principle of a partnership relationship of employer and employees in the plants and between their organizations above the plant level. (BDA 1955a: 7).

The BDA understood social partnership to be a way of containing the militancy and strength of the labor movement. This is evident from the way the BDA tried to define the rules of social partnership. *First*, the BDA emphasized that social partnership must be based on a balance of power between capital and labor. This referred primarily to the equal representation of capital and labor in corporatist bodies for the administration of social insurance programmes and labor market policies. A goal business could achieve, as is shown in the next chapter. *Second*, unions must limit their activities to those domains that, in the view of business, belonged to the proper competencies of the ‘social partners’: the negotiation of wages and working conditions. They should refrain from pursuing broader political goals.

Third, the BDA demanded that unions must be politically neutral and not take side in favor of any political party, nor must they participate in or fund any election campaigning. The BDA argued that any potential attempts by the non-partisan labor union federation (DGB) to cooperate with the SPD would destabilize the new parliamentary democracy. The BDA also considered the use of strikes for political purposes as against the rules and a serious threat to social partnership. Instead, unions had to limit themselves to bargaining with employers, whereby bargaining had to be limited to those issues that were within the proper domains of the social partners. Furthermore, co-determination at the firm-level, in particular, was seen as clearly beyond the legitimate domain of social partnership and in violation of capital ownership rights (see chapter 8). In short, the employer federation turned to social partnership as a tool for containing the potential militancy and power of the labor movement. Employers came to realize that social partnership would be a more effective way of containing the labor movement than confrontation.

The shift by business to social partnership was not mere strategy but reflects a real shift in the approach by German business to the labor movement. Evidence for this claim is

provided by the fact that German business after 1945 had supported a politically unified and non-partisan labor union federation, instead of politically fragmented union organizations. Before the World War I, industry had actively tried to split the labor movement by funding ‘yellow unions’ and other splinter groups (see Chapter 2). In the Weimar Republic the labor movement remained fragmented into political camps, with separate peak-level federations. A politically unified union federation could only be established after World War II. In 1951, Walter Raymond,¹¹³ the first president of the BDA (1949-1953) and a strong supporter of social partnership declared:

I personally believe that the unified [trade union] structure is better than having competing trade unions, since the reconciling of the natural differences of opinion, which are present in every large organization, is easier when the organization is committed to the retention of unity rather than to a competitive struggle. (BDA 1951: 30. translation from German by Bunn, quoted in Bunn 1959: 376).

A politically unified union organization may be more powerful than a politically fragmented one, but it provides business with a single bargaining partner, the prerequisite for effective and reliable bargaining. The support by the BDA of a unified trade union organization, and its lack of interest in a political fragmentation of the labor movement, can thus be seen as evidence of the credibility of the paradigm shift by German business. Unions had become fully recognized by employers as an equal bargaining partner. Bargaining and compromise-finding between capital and labor cannot be reliable and effective if one of the two sides is politically fragmented or if the representativeness of the organization of one of the two sides is in question.¹¹⁴

The new social partnership approach of the BDA was not universally accepted among all German industrialists, though. Authoritarian and paternalistic attitudes were still widespread among German industrialists during the 1950s, in particular in the traditional heavy industry (Berghahn 1985: 183). The manufacturing industries, in comparison, did traditionally pursue a more cooperative approach towards labor relations (see also chapter 2). The BDA leadership had therefore to take a mediator role between the old ‘hardliners’ of the heavy industry and their anti-labor attitude, on the one hand, and the labor unions, on the other hand. Both needed to be persuaded of the benefits of the new cooperative approach.

¹¹³ Walter Raymond, was an outspoken protagonist of the approach of ‘social partnership’. Unlike other business representatives, he did not have any leading position within the Nazi regime, neither within the NSDAP nor within the state apparatus, and represented a new compromise-oriented approach towards labor (Bunn 1960).

¹¹⁴ This observation confirms the hypothesis advanced by Karl O Hondrich and others that interest associations that represent antagonistic interests will try to strengthen each other, in order to justify their own *raison d’être* (Hondrich 1963: 43)

Also at the associational level, social partnership was not embraced by all. While the BDA embraced social partnership, the peak-level industry federation, the Federation of German Industry (BDI), remained more skeptical. The BDI remained particularly skeptical towards all types of corporatist institutions that involved a regulated and permanent form of bargaining with labor. The BDI enjoyed excellent informal contacts to officials in the relevant government ministries and preferred direct, bilateral cooperation between industry and government, thereby excluding labor¹¹⁵ (Braunthal 1965: 192-212). One important task of the BDA leadership during the 1950s was therefore ‘re-education’. Both, the labor unions and parts of business itself, needed to be persuaded of the benefits of social partnership.

Conclusions

In short, German employers resorted to the ‘social market economy’ as a programmatic alternative to communism and democratic socialism. The experiences of the Weimar Republic and the Nazi regime had seriously impaired the political legitimacy of unfettered capitalism and authoritarianism. At the same time, democratic socialism, with socialization and economic planning as its core elements, appeared as a serious and politically viable doctrine, advocated by the unions and the social democrats. The social market economy served as an attractive programmatic alternative by business. The doctrine of the social market economy was intended to provide political legitimacy to an economic order based on free market competition and private capital ownership. Although today the social market economy has become well-nigh synonymous to the welfare state, for its protagonists during the 1950s the concept meant almost the opposite. In the post-war context, the social market economy embodied economic liberalism.

As in the Wilhelmine Empire, social policy was part of the arsenal of weapons to be used in the struggle for the political legitimacy of the economic order. German business accepted social policies in principle as long as they could help to strengthen the political legitimacy of the liberal capitalist order, but it turned against policies that restricted entrepreneurial control over the use of capital. This was the case most clearly in the conflict over co-determination. The following two chapters analyze the response by German business to two reform initiatives with varying effects on entrepreneurial freedom: social insurance reforms and co-determination at the firm level. The two policies differ markedly in the way

¹¹⁵ The different positions of BDI and BDA appears to be largely the result of the different policy domains the two federations operated in. As the BDI dealt primarily with the product market interests of firms¹¹⁵ it had to interact much less with unions than the BDA and is thus likely to have perceived a necessity to accommodate to union strength.

they affect the rights of capital ownership: social insurance programmes leave the freedom of decision of capital owners unaffected: codetermination restricts the decision rights of private capital by transferring them partly to labor.

7 Post-War Social Policy Reforms: Containing Welfare Expansion

The immediate post-war period (from the late 1940s to the early 1950s) was characterized by rapid transformations in the political, economic and social spheres. The economic misery and mass poverty of the first post-war years (ca.1945-49) was followed by a period of rapid economic recovery, the famed ‘economic miracle’ (*Wirtschaftswunder*). The labor market situation changed from mass unemployment in the late 1940s to full employment in the late 1950s (Schmidt 1998: 68). The focus in social policy making changed as well. During the early post-war period policy makers focused on rebuilding the welfare state institutions that had been left financially broke by the Nazi regime. This period constituted a critical juncture that set the course for subsequent developments. Attempts to transform the Bismarckian welfare state into a system of universal social protection failed and set the path for a reconstruction of the old Bismarckian system of fragmented social insurance. After the old programmes had been reinstated in the late 1940s, the focus shifted to expanding benefit generosity, made possible by rapidly growing prosperity.

This chapter analyzes how employers have responded to key social policy reform projects during this period. Did employers’ endorsement of the “social market economy” translate into an endorsement for social policy reforms? How did employers respond to reform initiatives by other actors? On which kind of coalitions have these reforms been based? The chapter focuses on three core reform projects: First, plans for a transformation of the German welfare state from a Bismarckian system of social insurance to a universal system of so-called *Einheitsversicherung*; second, the conflict over parity representation for employers and unions within the re-instated institutions of social self-government; and third, the reform of the pension system in the 1950s, which improved benefit adequacy.

These three reform projects have been supported by different political coalitions. While in the case of the first two reforms employers prevailed, in the case of the pension reform they had to back down. The chapter shows that employers defended Bismarckian welfare state institutions against the challenge of a universalist welfare state system, indicating their preference for conservative social policies as opposed to universalist or social democratic social policies. Moreover, the third part shows that a weakening of employer

influence occurred as a result of a new dynamic of electoral competition that centered on welfare state expansion.

7.I Social Insurance Reform: The Conflict over Universalism (1945-1948)¹¹⁶

During the late 1940s Germany experienced an attempt to depart fundamentally from the path of a conservative welfare state that the country had embarked upon from the 1880s onwards. Bismarck's social insurance reforms during the 1880s had established a system of social insurance that provided earnings-related benefits to wage earners. Benefit rights differed between occupational groups, in particular between blue-collar and white-collar workers, and between private-sector employees and civil servants. The organization of social insurance was fragmented along occupational lines. The period of Allied occupation following the collapse of the Nazi regime provided a window of opportunity for a radical transformation of the German welfare state towards a universal and egalitarian 'people's insurance' system comparable to the system developed by Lord Beveridge in the UK. This attempt to transform the German welfare model ultimately failed and the old Bismarckian system was restored. Like in the cases of the introduction of social insurance in the 1880s and the introduction of unemployment insurance in 1927, (analyzed in chapters 3 and 5), employers had also this time preferred a Bismarckian system of occupationally fragmented and earnings-related benefits over more egalitarian and universalist alternatives. This section analyzes the conflicts over universalism and the reasons why employers opposed a universal 'people's insurance' model.

The occupation of Germany by the Allies after the war had created a critical juncture that opened up the possibility of a fundamental departure from the pre-existing path. The intervention by an external actor, the Allied Control Council (ACC), changed the range of policy options that were politically viable, because the Allies promoted institutional reforms. Two options were on the agenda: Continuation with the Bismarckian welfare state model or, alternatively, a shift to a universalist-redistributive 'unitary insurance' (*Einheitsversicherung*). *Einheitsversicherung* meant a system of social insurance covering the whole population (universal insurance) and applying the same benefit rules to all occupational groups (unified or unitary insurance).

The initiative for such a transformation to *Einheitsversicherung* came from the Allies. In September 1946, the Manpower Directorate of ACC had presented a proposal for a

¹¹⁶ This and the following section (I,II) rely in particular on the very detailed study by Hans Günter Hockerts(1980).

universal and unified social insurance system (Hockerts 1980: 26). The social democratic labor movement had traditionally demanded the introduction of universal ‘peoples’ insurance’¹¹⁷ (Hockerts 1980: 27, Fn.24.). The Allies considered the social democratic labor movement to be the representative of a dormant democratic tradition in Germany and were generally sympathetic to its political demands. Moreover, in 1946 the Labor government in the UK had enacted a pension reform inspired by the proposals of Lord Beveridge, which offered a template also for the reorganization of the German welfare state (Hockerts 1980: 27-31; Whiteside 2003: 23-32 re. the 1946 National Insurance Act in the UK).

The re-organization of social insurance proposed by the Allies in 1946 involved the extension of insurance coverage to previously uncovered groups such as the self-employed (“Selbständige”), uniform flat-rate benefits for all occupational groups and a centralization of the organization of social insurance. Instead of the plethora of insurance associations that existed so far, all programmes would be administrated by a single national authority, governed by the representatives of capital and labor. Remarkably, the Allies proposed that labor representatives should have two thirds of the seats and employers one third, a shift in power towards labor (Hockerts 1980: 37). Among the domestic actors, social democratic labor unions were the chief supporters of a universal *Einheitsversicherung*. The planned centralized organization and its governance by a labor majority would have provided substantial new power resources to the unions. Unsurprisingly, the shift in the balance of power was one of the key reasons why employers opposed the planned reorganization (see 7.II). But employers also had more fundamental objections about creating universal social entitlements, as shown below.

In the end, the proposal presented by the ACC failed. The reason for the failure was a combination of domestic opposition and the waning of support for reorganization among the Allies themselves. The Allies focused primarily on issues of foreign policy and defense, while issues of social and economic policies over time receded into the background. For several reasons the ACC began to withdraw from domestic economic and social policy issues from 1947 onwards¹¹⁸ and gradually delegated legislative powers in these areas to the Germans. For this purpose the ACC created the so-called ‘Economic Council’ (*Wirtschaftsrat*) in June 1947. The Economic Council was intended to function as a provisional parliament for the US

¹¹⁷ Demands for a universal and unitary insurance were made for instance at the SPD party congress 1902 in Munich, in the SPD Heidelberg programme from 1925 and in a resolution of the 1928 congress of the social democratic labor union federation in Hamburg (ADGB) (Hockerts 1980: Fn24 on 27-8).

¹¹⁸ The single most important reason has been the onset of the cold war and the intention of the Western Allies to tie Germany to the West, which lead them to avoid a heavy-handed approach.

and UK zones in the field of economic and social policy¹¹⁹ (Berghahn 1985: 209; Hockerts 1980: 86). The parties represented in the Economic Council were divided over the introduction of a universal *Einheitsversicherung*. The Social Democrats and the Communists, backed by the social democratic unions, favored a universal insurance programme. The non-socialist parties (CDU/CSU, FDP and DP), backed by employers, were in favor of keeping the traditional Bismarckian social insurance system. SPD and KPD held 46 seats and CDU/CSU, FDP and DP together 52 seats in the Economic Council. There was thus no majority in the Council for a transformation of the German welfare state towards a universal *Einheitsversicherung*¹²⁰ (Hockerts 1980: 88).

Given this disagreement about the future institutional form of the German welfare state, the factions in the Economic Council decided to divide the issues at hand into two parts. They agreed that the Council would only make decisions on urgent issues, such as benefit adjustments, while fundamental issues about the institutional form of the welfare state would be postponed, to be decided by the parliament of a future sovereign nation state. The Social Democrats accepted this postponement and refrained from putting their proposals for *Einheitsversicherung* on the agenda of the Economic Council. In December 1948 the Economic Council passed the so-called 'Social Insurance Adjustment Law' with the votes of SPD and CDU. This law raised benefit levels to counter the effects of inflation, but did not address the issue of institutional reorganization. The two parties had agreed on a lowest common denominator decision that left controversial issues open in order to be decided at a later point. The Social Democrats expected to win elections to the first sovereign national parliament, which would allow them to go ahead with their plans, supported by stronger political legitimacy (Hockerts 1980: 88).

The actual outcome of the first national elections thwarted this plan. In these elections Social Democrats and Communists together gained only 36.5 per cent of the vote (see table 7.1 below) (Alber 1989: 59). There was thus no parliamentary majority in favor of *Einheitsversicherung*. The non-socialist parties gained a majority and formed a coalition government, led by the Christian Democrats (CDU), with their party head Konrad Adenauer as Chancellor. The non-socialist coalition government decided to restore the traditional Bismarckian organization of social insurance. The labor wing within the CDU supported also this decision (Hockerts 1980: 131). This meant a return to a decentralized and fragmented

¹¹⁹ Initially, the Economic Council was only in charge of economic policy issues, in August 1948 its competencies were extended for social and labor market policy issues. (Hockerts 1980: 86-87)

¹²⁰ The total number of seats was 104. Even if the remaining six deputies would have supported an *Einheitsversicherung*, there would have been no majority for such a plan.

organization, privileged benefit rights for white-collar employees and corporatist self-government on the basis of parity between capital and labor (Hockerts 1980: 107-170). As a result, proposals for *Einheitsversicherung* were off the political agenda. The window of opportunity for a reorganization of social insurance had been closed.

Table 7.1 Seats in the German Bundestag (1949-today)

PARTY/ELECTION	1949	1953	1957	1961	1965	1969	1973	1977	1981	1985	1989	1993	1997	1999	2002	2005
Total number of deputies	402	487	497	499	496	496	496	496	497	498	497	662	672	669	603	614
CDU/CSU	139	243	270	242	245	242	225	243	226	244	223	319	294	245	248	226
SPD	131	151	169	190	202	224	230	214	218	193	186	239	252	298	251	222
FDP	52	48	41	67	49	30	41	39	53	34	46	79	47	43	47	61
Greens/ Alliance 90										27	42	8	49	47	55	51
PDS Left												17	30	36	2	54
Others	80	45	17													

Source: Wikipedia (2008)

Supporters and opponents of unitary insurance

The positions in the conflict over *Einheitsversicherung* followed by and large the class cleavage, pitting blue-collar workers against employers and white-collar workers. Support for a universal and unified insurance system came from the Social Democrats, the Communists and the social democratic blue-collar labor unions. In addition to industrial employers, opposition came also from the non-socialist parties, Christian unions, white-collar unions, the private insurance sector, artisans and medical practitioners (Hockerts 1980: 40-51). The social democratic labor unions did, in principle, favor a universal and unified insurance system, first, because this type of insurance system would result in a larger risk pooling and eliminate existing privileges of certain occupational groups, in particular white-collar employees and civil servants. A universal and unified system would cover all occupational groups and all risks (health, unemployment, accident and old-age) within one system.

Secondly, the governance of the proposed insurance organization was supposed to be based on a two thirds majority for labor, boosting the power resources of the unions. Opposition to some aspects of the ACC plan came also from within the labor movement,

especially to the benefit cutbacks included in the plan. On questions of institutional design of the new welfare state the social democratic unions did, however, support the principles of the ACC plan (Hockerts 1980: 426-427). The social democratic unions supported universal and unified institutions of social insurance because they eliminated occupational status privileges and created new power resources for organized labor (Hockerts 1980: 36-40).

Like the non-socialist parties, industrial employers resolutely opposed any form of unified or universal insurance system. Employers advocated the continuation of an occupationally fragmented system of social insurance, administered on a parity basis by capital and labor, and organized by decentralized insurance associations:

The Social Insurance Committee of the Confederation of German Employer Associations [the BDA, TP] in principle holds the position that the insurance principle within German social insurance must be maintained and must not be replaced or diluted by the principle of social assistance. It opposes a unitary social insurance ['Einheits-Sozialversicherung'] and favors the maintenance of the four independent branches of social insurance: work accident, pension, health and unemployment insurance. Within each of these branches, comprehensive self-government and far-reaching de-centralization...should be the strived for (statement of the BDA social insurance committee, quoted in Erdmann 1966b: 236, original source undocumented, translation and emphasis by TP).

Employers' opposition to universalism was motivated by several concerns. First, they feared an erosion of work incentives and work effort, if benefit entitlements would be granted as a matter of citizenship, rather than as a product of the employment relationship. They feared that universal insurance would "paralyze the self-reliance of the citizen to care for himself and his family" (BDA 1953a: 6). They viewed the Bismarckian model of social insurance to be more in line with the protection of work incentives and work effort than a universal welfare model, which would alleviate the individual too much from its responsibility to care for its own livelihood. Employers' defense of the conservative social policy model embodied in the Bismarckian welfare state, and their opposition to a universalist or redistributive model, lends support to the decommodification thesis (see p.31-2), according to which employers will oppose decommodification as a threat to work incentives and the employer's control over his workforce. They opposed *Einheitsversicherung* in part because they expected it to be more decommodifying than the Bismarckian model.

Organizational self-interests were a second reason for employers' opposition to *Einheitsversicherung*. Employers operated some insurance funds, either individually or collectively. Individual employers operated company health insurance funds. Employer associations operated accident insurance associations at the sectoral level (Hockerts 1980: 45). Both types of insurance associations operated within legal framework of social insurance. They were cherished by employers as 'a bridge for cooperation between entrepreneur and

workforce' (Hilbert 1947: 286), that is, as a tool facilitating cooperative labor relations. Due to their decentralized organization, they operated in proximity to the individual firm and were seen as being conducive to industrial peace. Furthermore, in the case of health insurance the narrow risk pooling involved in company funds also allowed firms to keep costs low. The unified and centralized insurance organization proposed by the Allies and supported by the social democratic unions would have meant the dismantling or crowding out of these employer-run funds (Hockerts 1980: 45).

Third, employers had an interest in maintaining the balance of power with unions created by the existing institutions. A centralized insurance administration would have created an organizational concentration of power in the hands of the labor unions, given the planned two thirds majority for labor in the governing bodies of social insurance. Employers criticized the ACC proposal as creating an 'excessive centralization of social insurance' and a concentration of power in the hands of labor (Schieckel 1947: 126). The proposal for a universal and unified insurance system was thus recognized by business as an attempt by labor to shift the institutional balance of power in its favor. In return, the unions accused business of trying to weaken the labor movement by denying a unified insurance system to labor. Fragmenting the working class into various occupational categories through the social insurance system meant fragmenting the labor movement also politically by obstructing the formation of a broad base of class solidarity, argued one union publication (Killat 1953: 87). In short, German employers preferred a welfare state based on the conservative-corporatist model to a welfare state based on a social democratic-universalist model (Esping-Andersen 1990: Ch.2; Titmuss 1958).

7.II Conflicts over the Balance of Power in Self-Government

Capital and labor participate in the administration of the German welfare state by what is called "social self-government" (*soziale Selbstverwaltung*). Social self-government is a defining characteristic of the Bismarckian institutions of social policy and shapes the institutional power resources available to both sides. Both sides cherished it, though in part for differing reasons. To the labor unions, self-government meant the transposition into practice of one component of their wider goal of 'economic democracy'. To employers it served more prosaic goals. Self-government offers employers a means of ensuring that payroll tax revenues would be put to use in a cost effective way and at the same time provides a forum for the cooperation with labor that tends not to be highly conflict-laden, as mentioned above. Although for somewhat different reasons, both sides considered self-government as

preferable to unilateral state administration. For both sides of industry the self-government of social policies was a source of political legitimacy and power resources that they did not want to forgo. Despite their joint preference for self-government, its re-establishment after the end of the Nazi regime was accompanied by intense conflicts between the two sides. This subsection provides a closer look at the main issue of conflict.

Since the introduction of social insurance in the 1880s, public social policies in Germany had been administrated by the social partners, instead of by the government. As a rule, capital and labor were represented in the governing bodies of the respective programmes in proportion to their share of contribution payments to that programme. In old-age insurance, for instance, capital and labor were represented on a parity basis, while in health insurance, labor had a two thirds majority, and work injury insurance was administrated by the employers alone, reflecting the respective share in contribution payments. A reform of self-government thus affected the vested interests of both sides. Parity representation meant that unions had to give up their majority in the administration of health insurance. Employers had to give up control over the work injury insurance associations, which they had been operating unilaterally at a sectoral level.

The Nazis had banned all independent forms of interest representation and had dismantled self-government. Instead, the administrative competencies affected were transferred to the government and the representatives of the two sides of industry were replaced with personnel loyal to the regime. This meant that after the end of the Nazi regime the organizational structures of corporatist self-government had to be rebuilt. Representatives of the Nazi party had to be replaced by representatives of the new social partner organizations, and institutional rules needed to be redefined. All this had to be done from scratch, as 12 years of Nazi rule and the social consequences of World War II had left the social insurance system financially bankrupt and organizationally in tatters (Schmidt 1998: 66-67).

The point of contention in the conflict over self-government was the distribution of power between capital and labor. Employers strongly favored parity representation, arguing that equality in strength would be essential to allow productive cooperation. The executive director of the BDA, Gerhard Erdmann, emphasized that ‘a true cooperation can not emerge if one of the two partners can dominate the other due to its superior number of votes’ (Erdmann 1966b: 295). The SPD and the union federation DGB demanded unilateral self-government by the insured groups, meaning the exclusion of employers (Hockerts 1980: 135, Fn.117). Briefly after the Economic Council had passed the Social Insurance Adjustment Law (see

above), the Council turned its attention to the issue of self-government. Two bills were introduced: The Social Democrats introduced a bill proposing a two thirds majority for labor; a bill which they considered as a compromise between the two positions. The Free Democrats (FDP) introduced a bill proposing parity representation, in line with the preference of employers (Hentschel 1983: 156; Hockerts 1980: 135).

The Christian Democrats appeared to be internally split between the labor wing and the business wing. The pivotal votes came from the labor wing of the Christian Democratic Party. Together with the votes of the SPD, the CDU labor wing would have provided a majority for the SPD's proposal. In the end, the labor wing of the CDU voted in favor of the FDP bill, providing a majority for parity representation (Hockerts 1980: 137). The Christian Democratic unions thought that parity representation would give employers a stronger stake in the governance of social insurance, facilitate productive cooperation between the two sides and thereby help to overcome class struggle (Hockerts 1980: 138 and 141-142). In short, with the support of the non-socialist parties (CDU+FDP) employers managed to win the conflict over representation in self-government.

The issue of representation had been so contentious because self-government provides both sides with important power resources. Control over personnel recruitment was one of the most important power resources provided by self-government. At the end of 1951, the organizations of social self-government employed about 80,000 to 90,000 persons (Hockerts 1980: 134-5). Unions and employer associations used the institution of self-government to allocate jobs to their officials. In particular for union officials, the organizations of self-government had thereby become an important tool for upward social mobility. In turn, the capacity to allocate jobs helped both sides to strengthen support among their members. In 1950, a leading DGB official criticized that "the employers and their supporters shall –that is their goal - dominate the administration of social insurance" in order for them to 'gain control over the personnel policy of the insurance bodies' (quote by Willi Richter, head of the department for social policy of the DGB and later president of the DGB, 1950, quoted in Hockerts 1980: 135). The salience of personnel recruitment as an organizational power resource was one of the main reasons why the conflict over self-government was so contentious.

Another key power resource was control over the use of insurance funds. Self-government provides the social partners with some influence over the usage of insurance funds. Clearly, the basic parameters that define the finances of social insurance are defined by

law: decisions about contribution rates, coverage and benefit formulas are made by the legislator and not by the social partners. Nevertheless, there is some discretion in self-government, for instance regarding the investment of reserve funds in the pension system and decisions about investments in hospitals, sanatoriums and other health care facilities in the health insurance system. In health insurance, the self-governing bodies can even change the contribution rate (Hockerts 1980: 134). Moreover, by participating in the administration of social insurance programmes, union and employer representatives could also gain valuable expertise and information that would make it easier for them to influence future debates about social policy reforms.

The support of German business for parity self-administration meant that it had to actively endorse cooperation with the unions. If parity self-administration was to work effectively, employer associations and unions had to cooperate. As all major parameters, in particular regarding contribution rates and benefit regulations, are decided by the state,¹²¹ self-government rarely requires the two sides to deal with issues that are politically highly conflict-laden. Instead, self-government deals with the relatively uncontroversial, technocratic issues of how to organize the administration of social policies and how to improve its cost effectiveness. Employers were happy to have a forum for the cooperation with organized labor in an area of activity that is rather technocratic in nature and tends to be low on issues of strong contention. This allowed the new strategy of social partnership to develop and created a counter-weight to the often contentious exchanges in the area of collective bargaining, where employer and union interests often oppose each other. Social self-government promised to ‘de-politicize’ the relationship between capital and labor and move the relationship into a more peaceful and technocratic direction. Even today, representatives of business and labor argue that cooperation in self-administration is functioning well and that existing ideological disagreements are tacitly kept away from the bodies of self-administration.¹²²

7. III The 1957 Pension Reform: Sidelining Business

The pension reform of 1957 was the first major welfare state reform in the Federal Republic. The reform raised pension benefits substantially, introduced wage indexation of pensions and enshrined financing on a pay-as-you-go basis (PAYG) in law. The economic recovery of the post-war period, the famed ‘economic miracle,’ had left the older generation behind. On

¹²¹ With the exception of the health insurance schemes, where the social partners have a say in determining the contribution rates

¹²² See also interviews with vice-secretary general of the Konrad Adenauer Foundation and with the head of the DGB social policy department

average, pension benefits in the 1950s were less than one third of the average wage (Hentschel 1983: 160; Schmidt 1998: 73). The pension system introduced by Bismarck in the 1880s intended to provide benefits merely as a supplement to other sources of support, such as family support, rather than covering the full costs of living. Before the 1957 reform, the benefits paid by the public pension system were often insufficient to lift the retired above the poverty level. The policy goal of the 1957 pension reform was to raise the standard of living among the retired and thereby to allow them to participate in the rapidly rising prosperity of the working population.

The 1957 pension reform was strongly affected by the dynamic of electoral competition between the two major parties, the Social Democrats (SPD) and the Christian Democrats (CDU/CSU). The reform project was initiated by Chancellor Adenauer (CDU), who decided to attempt a major welfare state reform in order to enhance popular support for the new Federal Republic and for his non-socialist coalition government in particular. Both parties were vying for pro-welfare votes. The proposals for a reformed pension system presented by the government and the oppositional SPD turned out to be remarkably similar (Hockerts 1980: 352-362). The reform was passed by the national parliament on January 22nd, 1957 with the votes of the governing CDU/CSU and the oppositional SPD, while the CDU's coalition partner, the Free Democrats (FDP) voted against (Hockerts 1980: 421). Unlike the reforms of the late 1940s (section I+II), this reform was not so much characterized by a programmatic left-right divide, but by electoral competition instead.

With hindsight, the 1957 pension reform appears paradigmatic of the dynamic of social policy expansion that characterized the post-war period. Social policy expansion had become an instrument of electoral competition (Alber 1989: 254ff). Not only the SPD but also the CDU/CSU vied for the votes of the large group of wage earners. The Christian Democrats, as the main center-right party, relied on a very heterogeneous voter base, which comprised a large labor wing. In order to gain votes, the Christian Democrats decided to support social policy expansion. As a result, the expansion of social policy in the post-war period was in general supported by both parties. Out of 68 key social policy laws adopted between 1950 and 1983, 39 were also supported by the main opposition party, whereby most of these laws concerned the expansion of social policy (Alber 1989: 262, Table 43). Electoral competition had turned both of the two major parties into 'welfare state parties' and had resulted in the receding of the old programmatic cleavages.

Employers had unanimously opposed the 1957 pension reform. Despite powerful support from within the government and the *Bundesbank*, employers had little success in changing the reform according to their preferences. Employers directed their efforts against the planned mode of pension indexation. At stake was the choice between wage indexation, as advocated by the government and the SPD, and a weaker form of indexation linked to productivity gains, as proposed by the employers. This section analyzes the reasons why employers had opposed the 1957 pension reform and how the new dynamic of electoral competition had resulted in a sidelining of employer interests. This sidelining motivated employers to intervene in the policy-making process with their own alternative proposal for pension indexation. The next subsection gives a brief overview of the reform process, before turning to the role of business in the subsequent subsections.

The reform process

The pension reform of 1957 emerged from earlier plans by Chancellor Adenauer to develop a master plan for a comprehensive reform of the German welfare state. The social policy of the first Adenauer government (1949 – 1953) was characterized by policy improvisation, resulting in a patchwork of various measures. The priorities in this period were to rebuild the old institutions of Bismarckian social insurance and to address the pressing social needs that resulted from the war, including support to refugees, displaced persons and war victims. These tasks had largely been accomplished by the end of the first legislative period in 1953 (Schmidt 1998: 69-72).

The 1953 elections had further strengthened the Christian Democrats (see table 7.1 above) and resulted in the reconstitution of the non-socialist coalition government, again led by Konrad Adenauer as Chancellor. The CDU-led government came under pressure to act after the SPD had presented a comprehensive ‘social policy master plan’ in 1952. This plan included proposals for a tax-financed national health service, full employment policies and a tax-financed, universal flat-rate pension system (Hockerts 1980: 220-222). The SPD and the CDU agreed on the need for a comprehensive overhaul of the existing social policy legislation, in order to simplify existing laws and make regulations more coherent. Attempts to draft a joint plan failed, however, due to the different policy positions of the two sides and the dynamic of electoral competition. The SPD favored tax-financed, universal social policies; the CDU favored contribution-financed insurance policies, maintaining the existing Bismarckian system of social insurance (Hockerts 1980: 223-231). In short, in terms of the typology of Richard Titmuss, the SPD advocated the “institutional-redistributive model” of

the welfare state, while the CDU advocated the “industrial achievement model” (Titmuss 1958).

In his inaugural speech for his second four-year term in office in October 1953, Chancellor Adenauer promised a comprehensive and all-encompassing reform of the German welfare state. He promised that the government would develop a ‘master plan for social reform’, covering all areas of social policy (Hockerts 1980: 242-243). The patchwork of reforms enacted during his first term in office had made the regulations of the already fragmented welfare state exceedingly complex and confusing. The envisaged master plan was intended to simplify existing legislation and make the existing rules more coherent and systematic. Its goal was to design a ‘social insurance system of one piece’. Moreover, the comprehensive reform was also intended to benefit in particular those that were unable to work, in particular the retired and disabled persons. Thereby, these groups should be enabled to participate in the rapidly rising social prosperity.

The development of the announced master plan did not, however, make any headway and was eventually abandoned. Internal conflicts within the government and inter-ministerial rivalries obstructed the reform progress. The first two years the government was preoccupied with procedural questions. Who would be in charge of developing the envisaged master plan? The Ministries of Economics and Finance were at loggerheads with the Ministry of Labor. On the surface, the point of contention was the planned establishment of an inter-ministerial government commission to develop the envisaged master plan (Hockerts 1980: 248). The Ministry of Finance insisted on such a commission in order to avoid that the master plan would become the sole competence of the Ministry of Labor. The appointment of the commission failed due to resistance from the Ministry of Labor. This conflict over competencies was influenced by deeper goal conflicts between the ministries involved. The Ministry of Finance had a keen interest in promoting the idea of means-testing in the reform process in order to reduce social expenditures, while the Ministry of Labor insisted on the importance of an earnings-related system of social insurance (Hockerts 1980: 297; Hentschel 1983: 161-162). As a result of these inter-ministerial conflicts over competencies and goals, the idea of developing a ‘master plan for social reform’ was eventually abandoned.

After the failure of the master plan the government decided to set its sights lower and narrow down the envisaged reform project. Given that the time left until the next parliamentary elections was running out, the government felt under increasing time pressure to act. Adenauer was determined to present a social policy reform in time for the 1957

elections in order to be able to challenge the Social Democrats in their position as a protagonist of social protection. The Social Democrats had presented a new pension reform plan in September 1955. The SPD had decided to put its earlier demands for a universal pension system on the back burner and was now focusing its demands on benefit improvements within the existing programme, instead. In the summer of 1955 Adenauer took the initiative to narrow down government plans to the area of pensions (Hockerts 1980: 307). Pension insurance was by far the largest programme in terms of the number of recipients. Moreover, poverty was concentrated among pensioners. Therefore, an improvement of pension benefits appeared to be suitable to appeal to a large part of the electorate.

Adenauer tried to overcome the stagnation of the reform process by bringing in advice from external experts. Already in the spring of 1955 he had mandated a group of academics to draft a proposal for the envisaged social policy master plan. This report, known as the 'Rothenfels memorandum,' proposed far-reaching changes to the German welfare state. Among other things, the report proposed to base pension finances on pay-as-you-go financing (Achinger 1955: 107-9). This report was, however, considered too radical within the government and was not followed up. The blueprint for the 1957 pension reform came instead from another academic: Wilfried Schreiber, an economist affiliated with Catholic social teaching (Schreiber 1955). Schreiber's pension plan gained the keen interest of Adenauer, who invited Schreiber to present his plan to a cabinet meeting in December 1955 (Hockerts 1980: 316-318). The 'Schreiber plan' became the blueprint for the pension reform adopted by parliament in January 1957.

Building on the Schreiber plan, the 1957 pension reform was characterized by three elements. First, pay-as-you-go financing became enshrined as the method of financing the pension system, basing the political legitimacy of the pension system explicitly on the notion of an inter-generational contract. Second, existing pension payments received a one-time increase of about 65 per cent for blue-collar workers and 72 per cent for white collar workers. Third, pension credits and pension benefits became indexed to the growth of gross wages. In effect, a person with an average wage and 40 years of employment was entitled to a pension of 60 per cent of its wage at the time of retirement (Hentschel 1983: 165).

By linking the value of pensions to wage growth, this so-called 'dynamisation of pensions' was intended to make sure that the standard of living of the older generation would develop in line with the standard of living of the working population, which was rising rapidly due to the prosperity created by the 'economic miracle'. Moreover, wage indexation in effect eliminated the effects of inflation on pension benefits. Before the reform, entitlements for

pension benefits had been calculated on the basis of the nominal value of the contributions paid by a person throughout his or her working life. In addition, pensions had not been subject to any automatic indexing but were instead adjusted occasionally through discretionary decisions by the parliament. As a result, pension benefits were vulnerable to devaluation due to inflation, unless parliament granted an adjustment of benefits. In effect, the pension reform of 1957 removed the risk of devaluation from pensioners.

The role of business in the 1957 pension reform process

The reform succeeded despite the united opposition of industrial employers, the insurance and banking sector, the central bank and its president (Vocke), as well as the Ministries of Finance (Schäffer) and Economics (Erhard). Opposition to the reform was spearheaded by the banking and insurance sector, which feared a crowding out of private pension provisions. In September 1956 associations of the banking and insurance sector joined forces to form the 'Society for the Protection of German Savers'. The purpose of this group was to campaign against the 'dynamic pension' (Hockerts 1980: 378). Opposition was directed primarily against wage indexation, furthermore also against the one-time increase of benefit payments and against the extension of compulsory coverage to white-collar employees above a certain salary threshold, who had previously been excluded (Hockerts 1980: 376). The third part of the reform, the introduction of pay-as-you-go financing, was supported by the employer federation (BDA). The BDA justified pay-as-you-go financing on the grounds that a pre-funded public system would lead to the concentration of financial power in the hands of centralized pension funds:

The accumulation of reserve funds that results from pre-funded financing poses specific problems to the national economy, both relating to the investment as well as to the later disinvestments of capital. In addition, the accumulation of substantial capital funds gives the insurance institutions the character of credit institutions, with all the accompanying economic and political side effects. For the purpose of securing future benefit rights, it is..., however... not decisive, whether this securing occurs through pre-funding...or...is taken ... from the current national product. (BDA 1955b: 21).

The employer federation accepted that an increase in the purchasing power of pensioners was necessary, but insisted that this should not be accomplished through any form of automatic wage indexing. The BDA justified its opposition to wage indexation with macroeconomic arguments. These arguments can be summarized by the following three points: (i) wage indexation exacerbates inflationary trends, (ii) crowds out private pension provisions and (iii) increases labor costs unduly (BDA 1955b: 19-21; 1956: 23-26).

First, the BDA argued that automatic wage indexation of pensions would be likely to lead to higher inflation by extending the impact of inflationary wage agreements to pensioners. In effect, wage indexation results in the value of pension benefits being decided by collective bargaining. Hitherto, pensioners had a strong political interest in currency stability, as their pension benefits were calculated on the basis of the nominal value of their contribution payments made in the past, instead of their current value. With the reform, pensioners would lose their political stake in currency stability and their economic interests would become tied to those of labor: 'If now the army of pensioners gets politically tied to the interests of the wage earners, this will result in a political shift that is extraordinarily dangerous' said one banker (Hugo Scharenberg, Hamburg, at the meeting of the CDU executive board on September 20th, 1956, quoted in Hockerts 1980: 380).

Fears about inflationary wage increases were given credibility in particular by the announcement of the labor union federation DGB in 1955 to pursue a so-called 'active wage policy.' Active wage policy meant wage increases above the level of productivity increases (BDA 1956: 12; Erdmann 1966b: 269). The BDA's annual report for 1956 summarizes the concerns of German employers about the inflationary effects of the 'dynamic pension'

Recent wage and salary increases have gone significantly beyond the increase in productivity. This development... will be exacerbated by a pension dynamisation linked to wages. In the future, wage conflicts will also be about pension increases. Then, the wages will force up the pensions, and the pensions will force up the wages, and both together will force up the prices. (BDA 1956: 25, translated by TP)

As an alternative to wage indexation, employers proposed to adjust pension benefits by discretionary decisions made by an expert committee, which would make its decisions on the basis of productivity developments (see below).

Second, business feared an erosion of private savings due to the suspected crowding out of private pension provision by the public pension system. As a result, an 'an important source of capital formation would be exhausted' (BDA 1956: 25). The fear that a generous and inflation-proof pension would undermine the formation of investment capital was widespread also among German economists. The prevailing economic orthodoxy was monetarist and the influence of Keynesian ideas of demand management was very limited. This implied that economic policy focused on facilitating investments in the exporting sectors and not on boosting domestic consumption. Economists and economic policy makers gave priority to capital formation to boosting consumer spending (Shonfield 1965: 272-6). With hindsight, these fears about a depletion of private investment capital have turned out as

invalid. Since the introduction of the ‘dynamic pension’, aggregate private savings did in fact increase rather than decrease (Schmähl 2004: 164).

Third, business was concerned about the reform’s effect on labor costs. Employers suspected that the financial costs of the reform would be substantially higher than what the Ministry of Labor had estimated. Different actuaries came to significantly different results regarding the expected costs of the reform, something the opponents of the reform tried to exploit by pointing out the massive uncertainty about the financial sustainability of the reform. The government projected that for the first ten years a contribution rate of 14 per cent would be sufficient, compared to 11 per cent in the old system. For the two decades thereafter an increase to 16.25 per cent would be necessary (BDA 1956: 23). Relying on a study by a different actuary, the BDA estimated that the required contribution rate would be as high as 24.2 per cent in 1986 and 29.5 per cent in 2001, instead (BDA 1956: 24) (Heubeck 1956). To compare with, the actual contribution rate in 2001 had been at 19.1 per cent (Schmähl 2003: 132, Table 5.5). In short, the financial sustainability of the new pension system in the face of demographic ageing was already an issue among actuarial experts at that time and was one of reasons why employers opposed the reform (Hockerts 1980: 385-387).

Failed alternatives

Business confronted a “grand coalition” of Christian Democrats, Social Democrats and labor unions in favor of the “dynamic pension”. This compelled the opponents to come up with alternative proposals in order to avoid becoming irrelevant bystanders to reform project that appeared as unstoppable. The employer federation BDA and the private insurance sector presented two substantially different proposals. The proposal made by the employer federation BDA intended to took the edge out of the reform by changing the adjustment procedure. Instead of the quasi-automatic form of wage indexation proposed by the government, the BDA proposed a form of discretionary adjustments. Decisions about increases of pension credits and pension benefits should be made by an expert committee on the basis of the development of labor productivity. The proposal suggested adjustments to be made every 5 years. The expert committee should include experts nominated by the government, the unions and the employers themselves (BDA 1956: 221-225; Hockerts 1980: 331-332). The proposal thus meant that pension adjustments would not take place automatically, but would, instead, be subject to the discretionary decisions of experts. Employers hoped that adjusting pensions by discretionary expert decisions, instead of by

automatic indexation, would create a means of countering inflationary developments and help to limit the expected rise in labor costs.

In a surprising about-face, the private insurance sector presented a radically different proposal. In May 1956, the 'Association of Private Life Insurers' came forward with a proposal for what it called 'flexible basic citizen pension.' According to this proposal, every citizen should receive a uniform flat-rate pension, which would provide a minimum living income and would from time to time be adjusted to 'economic progress' (Bauer et al. 1956). The motivation behind this proposal is manifest. A basic pension system is less likely to crowd out private pension provisions compared to an earnings related system, and therefore provides ample room for private pension provisions to prosper.

The proposal, if implemented, would have meant a radical shift of the German pension system from the Bismarckian model to the Beveridge model, from earnings-related benefits to universal flat-rate benefits. The proposal came very late in the reform process and stood no chance of success. Of all parliamentary factions, only the Free Democrats (FDP) were sympathetic to the proposal (Hockerts 1980: 387-388). It reflects, however, a remarkable departure of the life insurance sector from the position of business in general. The life insurance sector was now propagating precisely the kind of universal basic pension that the Social Democrats had propagated earlier, in the late 1940s and early 1950s, but had failed to introduce due to the massive resistance from all segments of business at that time. Now, a cross-class alliance in favor of a universal basic pension system could not materialize, as the Social Democrats had shifted their priorities, away from universalism and towards an incremental reform of the Bismarckian pension system.

In contrast to the insurance sector, the employer federation supported the Bismarckian model of the welfare state and opposed a fundamental transformation of the welfare state towards a liberal or universalist model. The BDA was aiming at containing pension expenditures, but it wanted to achieve this within the existing framework of the Bismarckian welfare state, of a welfare state that provides earnings-related benefits rather than universal flat-rate benefits:

Due to the legislative development, the boundaries between *insurance*, *social welfare* and *social assistance* have become strongly blurred. The task of a social reform is to again create clear distinctions and to decide in favor of one single principle. [The BDA] declares its commitment to social insurance and the insurance principle, which creates legal entitlements on the basis of a *quid pro quo* of contributions paid and benefits received. ['Leistung und Gegenleistung']. (BDA 1955b: 20, emphasis in original.)

The different positions taken by employer federation and insurance industry are rooted in different preference orderings. Both groups had a strong interest in containing pension expenditures and limiting benefit generosity, albeit for somewhat different reasons. The insurance industry wanted moderate benefit levels in order to leave enough scope for private pension provisions. The employer federation wanted moderate benefit levels in order to limit labor costs. However, the BDA, representing the *labor market* interests of firms, additionally had a strong interest in limiting the decommodifying effects of social policy in order to maintain work incentives. The BDA preferred the Bismarckian to the Beveridge model, because only an earnings-related system maintained the market distribution of income and thereby guaranteed the maintenance of work incentives and work effort. A universal benefit system in contrast was suspected to undermine work incentives by liberating workers from the need to work (see also chapter 5).

In short, the interests of employers in general were more complex than those of the insurance sector. The insurance sector merely wanted to carve out a space for private pension products, and therefore advocated a limited role for the state in pension provision. In comparison, employer interests were less straightforward. They had to combine their interest in containing pension expenditures with their interest in maintaining work incentives. Employers viewed a sound reward structure as essential for the maintenance of work incentives and the economic recovery of Germany, as the recovery could only be achieved by way of hard work. In their view, an overly decommodifying welfare state would have destroyed the foundations of economic prosperity by eliminating work incentives. Their interest in avoiding decommodification prevented German employers from advocating a radical transformation of the German welfare state towards a universalist flat-rate model. The case of the 1957 pension reform thus confirms the hypothesis that employers' preference for conservative social policies is motivated by their interest in maintaining work incentives.

Despite support from within the government and the central bank, employers did not prevail in the reform process. Business made intense efforts lobbying against the reform, such as the activities by the 'Society for the Protection of German Savers', the insurance sector's lobbying group. In June 1956 BDA president Paulssen met personally with Chancellor Adenauer to urge the government to abandon plans for automatic wage indexation. The government bill presented briefly after discounted employers' objections and stuck to wage indexation. In response, Paulssen wrote a letter to Adenauer in September 1956, in which he again reminded the Chancellor of the BDA's objections. He received a reply by the Ministry

of Labor's undersecretary of state. The reply dismissed the objections and the alternative proposals made by the BDA. In October 1956, Paulssen and BDA executive director Erdmann met again with Adenauer. Adenauer informed the employer representatives that an internal group would currently work out regulations to avoid negative economic repercussions. An offer by Adenauer to forward an exposé drafted by Erdmann to this group was all the employer representatives could achieve (Hockerts 1980: 391-392). In sum, employers failed to leave their mark on the reform outcome. In its 1957 annual report, the BDA expressed its disappointment:

Regarding the core question in the reform of the public pension system, the pension formula, the majority of the parliament has in principle supported the automatic linking of pensions to the development in wages and salaries, regarding the determination of the first pension. The parliament has thus defied the objections made by various sides – including also by the Confederation of German Employer Associations – against such a linking of pension developments to wage developments regarding the threat to the purchasing power of the DM [Deutsche Mark] and the excessive demands made on the [wage bargaining] autonomy of the social partners (BDA 1957: 224, translated from German by TP).

The role of business in the 1957 pension reform was one of reluctant acceptance. During the final plenary debates in the parliament, employers refrained from articulating their opposition, given the clear majority in favor of the reform. After business had won the fight against the unitary insurance in the late 1940s, its focus shifted towards taking the edge out of expansionary reforms. In the debate over the introduction of the 'dynamic pension' business was sidelined, although it was actively campaigning against the reform. Except for some smaller concessions regarding the scope of compulsory coverage, business failed to prevail.

The sidelining of business was the result of the dynamic of electoral competition between the Social Democrats and Christian Democrats. Both parties were vying for the votes of wage earners and pensioners. The CDU contained a strong labor wing and was thus receptive to plans for social policy expansion. The SPD and the CDU both supported the wage indexing of pensions. The Social Democrats had presented their own reform proposal, which was however remarkably similar to the government's own bill. For reasons of electoral competition, the Social Democrats had put their earlier objective of a radical transformation of the German welfare state on the back burner and had shifted their focus to demands to incremental benefit improvements instead.

Adenauer felt that the government was under pressure to present a major social policy reform before the 1957 elections and decided to take a more active role in the reform process to ensure the timely passing of the reform. Despite of his close ties to the president of the Federation of German Industry (BDI), Fritz Berg (Braunthal 1965: 193), he had in this case

appeared not to be susceptible to the preferences of industrial employers. In short, under the influence of electoral competition, the social policy positions of SPD and CDU/CSU had converged. Electoral competition had outpaced ideological confrontation. Given their limited electoral weight, employers were sidelined.

Conclusions

The debate over institutional reform in the early post-war period required employers to show their colors: Employers came to defend the Bismarckian welfare state in a situation where it was at risk to be replaced by a more egalitarian universalist model, as favored by the Social Democrats and the labor unions. Like in the case of unemployment insurance (chapter 5), employers preferred conservative social policy to universalist social policy. In other words, they preferred status protection and corporatist self-administration to egalitarian benefits and direct state administration. This finding confirms the importance of the protection of work incentives to employers, as emphasized by the decommodification thesis, as conservative social policies protect work incentives better than universalist social policies.

Struggles over the institutional balance of power between capital and labor in social insurance administration played also a central role in this conflict. The first sovereign post-war government, a non-socialist coalition led by the Christian Democrats, reconstructed the Bismarckian welfare state programmes in line with the preferences of employers and Christian democratic workers. The proposals for a universal and union-administered social insurance system had been defeated by an alliance between the non-socialist government parties and employers, whereby the pivotal votes came from the Christian-Democratic labor wing.

Once questions of organizational design had been sorted out, the focus of politics shifted to benefit expansion, something that pushed employers to the margins. Issues of benefit adequacy turned out to be ideologically far less divisive and followed an altogether different logic of policy-making. The centerpiece of these reforms was the introduction of so-called “dynamic pension benefits” in 1957. This reform was characterized by a convergence of positions between Christian Democrats and Social Democrats, driven by electoral competition between the two parties. This resulted in a sidelining of employers in the reform process. Again, the reliance of the CDU on a strong labor wing within the party had played an important role. This time, however, the CDU’s diverse class base worked against employers and led the party to pursue a policy of welfare state expansion, made possible by the rising

prosperity of the 'economic miracle'. The resulting convergence of the two main parties on issues of welfare state expansion sidelined the objectives of employers, who had to reconcile themselves with the new reality.

To conclude, the changing dynamics of welfare state politics had compelled employers to accommodate to a new political situation. During the organizational reforms of the late 1940s, employers had a parliamentary majority on their side and did thus not need to make any compromises. They could rely on a favorable parliamentary majority to defeat proposals for a transformation of the German welfare state from a conservative to a universalist-social democratic model. In contrast, the pension reform of 1957 confronted employers with a broad parliamentary majority in favor of reform. Employers had lost the CDU as their parliamentary ally. While the CDU opposed the plans for organizational reform during the late 1940s, the party supported the pension reform of 1957. Employers were thus left without a strong parliamentary backing. They decided to accommodate and presented alternative reform proposals as "lesser evils". The new dynamic of electoral competition confronted employers with new political constraints and led them to moderate their positions, though with only limited success.

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An important exception to employers' politics of accommodation constitutes the case of co-determination. While employers reluctantly accepted the expansion of the welfare state in the face of political constraints, they fought adamantly against the introduction and extension of codetermination, even when the political odds were clearly against them. The case of codetermination provides a remarkable deviation by employers from the politics of accommodation. The following chapter looks at what made codetermination special to employers, what motivated employers not to back down in this case but to seek open confrontation instead.

8 Codetermination: Employers against Economic Democracy

‘Its [codetermination’s] decisive characteristic is its aim to abolish private property as the means of production (as is the aim of Marxism); its method is evolutionary (differing from Marxism, the method of which is revolutionary)’

Statement by Walter Raymond, president of the BDA (quoted in BDA 1953b: 268)

It is often argued today that codetermination (*Mitbestimmung*) is a competitive advantage for German firms, contributing to a loyal and motivated workforce, improving communication between workforce and management and facilitating workforce restructuring (e.g. Jackson 2005: 234-5; Streeck 1992: 137-68). This perspective stands in sharp contrast to the attitude of industrial employers to codetermination. Employers fought tooth and nail against the introduction and subsequent extension of codetermination. What were the goals of the protagonists of codetermination and why had they been so adamantly opposed by employers? And why did employers not manage to prevent the institutionalization of codetermination despite their best efforts? Had German employers subsequently changed their attitudes towards codetermination in the light of their practical experiences with this institution and, if yes, in which way? This chapter analyzes the political struggles that characterized the introduction and subsequent development of the institution of codetermination and the role played by employers therein.

The term *codetermination* stands for the representation of worker interests in decision-making within firms on the basis of equality (parity) with owners.¹²³ Today, codetermination forms an integral part of Germany’s so-called ‘dual system’ in industrial relations. The two parts of this system are (a) the representation of worker interests at the level of the individual firm, by the works councils and codetermination in the supervisory board of larger firms and (b) the system of collective bargaining between unions and employer associations at the sectoral level. Together, these institutions underpin the system of industrial relations in the Federal Republic. As shown in chapter 4, works councils and sectoral collective bargaining

¹²³ The concept is sometimes also used to include the works councils, which represent worker interests at the workplace level (Katzenstein 1987: 125; Thelen 1991: 63-83). In this chapter the concept of codetermination is used to refer only to institutions of employee participation at the firm level. Employee participation at the workplace level, through the works councils, is not analyzed in this chapter, neither are forms of labor-capital cooperation at the regional, sectoral and national level.

were already introduced in November 1918 as part of a more encompassing deal between capital and labor to defeat a revolutionary threat. Codetermination in the supervisory boards was added to the dual system after World War II, forged out of political struggles between capital and labor during the early post-war years.¹²⁴

The outcome of these struggles was the legislation of codetermination in two different variants in the early 1950s. The so-called *Montan Codetermination Law* of 1951 defined codetermination rules in mining, iron and steel. The law instituted parity representation in the supervisory boards of firms in these sectors, giving one half of supervisory board seats to the representatives of labor and the other half to the representatives of capital owners. In addition, the law instituted a special ‘labor director’, who is a full member of the firms’ executive board and whose appointment can be vetoed by the labor representatives. The second variant is enshrined in the so-called *Works Constitution Law* of 1952. This law instituted a weaker form of codetermination for firms with more than 500 workers outside of mining, iron and steel. The law gave labor representatives only one third of supervisory board seats and no veto over the appointment of the labor director. Codetermination in its fully-fledged form, i.e. *parity* codetermination, was thus only instituted in the heavy industry. In 1976 a new law extended codetermination rights in very large firms outside of the heavy industry. While the weaker codetermination rules of the 1952 law were acceptable to employers, they adamantly opposed the parity variants of codetermination as defined by the 1951 and 1976 laws. Unions, in contrast, viewed the 1951 law as a success and the 1952 law as a massive defeat, while being disappointed also by the rules of the 1976 law (Thelen 1991: 64; Thum 1982: 146-9).

This chapter is structured as follows: The first section analyzes the positions taken and the arguments used by unions and employers in this conflict and thereby puts it into the context of the wider programmatic disagreements between the two sides about the proper political-economic order of Germany. The second section looks at how the two laws came about and why employers were so much less successful to in the case of the 1951 law than in the case of the 1952 law. The re-emergence of the codetermination conflict during the 1970s is analyzed in section three. Section four deals with the positions of employers to codetermination today.¹²⁵

¹²⁴ A rudimentary form of codetermination at the firm level already existed in the Weimar Republic. A supplementary law to the 1920 Works Council Law, passed in 1922, entitled the works councils to two representatives in the Supervisory Board. This provision was strongly opposed by the employer associations.

¹²⁵ The purpose thereby is not so much to give a full account of how codetermination emerged and developed over time, but to explore the reasons for the intensity of the controversies that accompanied its introduction and development.

8.I Codetermination and the Economic Order: The Positions of Employers and Unions

Codetermination is an example of an institution that is characterized by a sharp difference between the objectives that originally motivated its formation and the practical results it produced over time. At the time codetermination was introduced it had a very different meaning to political actors from what it would come to assume later. The issue of codetermination pitted the political programmes of employers and unions regarding the proper political-economic order of the Federal Republic against each other. This section analyzes the positions taken and the arguments used by both sides and thereby intends to demonstrate what kind of political-economic order German industrialists embraced and what kind of order they tried to prevent.

Employers and unions initially disagreed fundamentally over what kind of political-economic order the new Federal Republic should be based upon. During the 1950s, the labor movement had by no means reconciled itself with the social market economy advocated by Ludwig Erhard and industrialists. Instead, the labor movement wanted to transform the West German political-economic order on the basis of the socialization of key industries, economic planning and codetermination. These three components were understood as parts of a larger programme and together should ensure the democratization of the economy. Codetermination was thus not seen as an end in itself, but as a means towards a larger goal. Unions argued that just as all citizens have equal voting rights in the political sphere, business and labor should be entitled to equal voice in the economic sphere. They should thus be represented equally in the decision-making bodies at all levels of the economy (DGB 1950: 27). Through their involvement in codetermination and in economic planning institutions the labor unions would play a pivotal role in the new political-economic order. This pivotal role for the unions was justified on the grounds that unions would act as agents of the common good, rather than merely of the self-interests of their members (Hondrich 1963: 80-1; Thum 1982: 18-20).

These proposals were inspired by the programmatic concept of '*economic democracy*', developed by labor union intellectuals during the Weimar Republic. They intended economic democracy as a third way between unfettered capitalism and the bureaucratic centralism of Soviet communism. One of the main protagonists of this programme was the social democratic unionist Fritz Napthali. His programme for the democratization of the economy was officially endorsed by the national congress of the socialist labor union federation (ADGB) in 1925 (Berghahn 1985: 206-207). Napthali understood economic democracy as an

intermediary step towards socialism. Socialism was the ultimate goal, economic democracy the proximate goal (Napthali 1928):

Socialism and economic democracy are twin goals inseparably linked together. There can be no fully developed economic democracy without a socialized economic system and the ideal of socialism cannot be realized without the democratization of economic control. If, in spite of the unity of the twin goals, the idea of economic democracy expands, it is because the new, concrete conceptions about the way to realize socialism are bound to the new social structure. The purpose and goal of socialism has remained essentially unaltered in the modern labor movement. The notions of the way leading to this goal have been changed in accordance with the growth of the labor movement and the transformations which have taken place in capital structure...The means for realizing socialism are through the democratization of the economy' (Napthali 1928: 16, translated by Bunn, emphasis added by TP).

In the view of Napthali, the establishment of a socialist system required the democratization of the economy. As, for the moment, a socialist state was politically not feasible, the process of democratizing the economy had to start already within the capitalist system. According to Napthali, an important tool for democratizing the economy would be the codetermination of business policies by capital and labor. The democratization of the economy required the limitation of the amount of control of capital owners had over their firms:

The nature of democracy requires codetermination by the workers. Works councils, self-administration in social insurance...are only steps on the way towards this goal...*Economic democracy means the restriction of the entrepreneur in his discretion over his means of production.* A democratic economic order is impossible without a change in the relations of ownership. There is no economic democracy without a socialist economic system. Political equality does not equal true equality of the workers (Napthali 1928 , emphasis added by TP).

After World War II, the labor movement returned to this programme with new fervor, now reassured by the disastrous experiences made during the Weimar Republic and the Nazi era that a democratization of the economy would be of paramount importance to prevent the reoccurrence of past experiences. In contrast to the Weimar Republic, the labor movement now tended to tone down its teleological Marxist rhetoric, and instead argued that the establishment of economic democracy would be justified by the goal of avoiding another collapse of political democracy. The labor movement understood the rise of Nazism in the 1930s as a result of the economic instabilities produced by capitalism and the role played by heavy industrialists in helping Hitler to come to power (Rosenberg 1953: 6).

The labor movement viewed the political, economic and social disasters of the Weimar Republic, which paved the way for the Nazi regime, as a result of the inability of the masses to influence the decisions of the industrial elites. In its view, the collapse of Nazism implied also the collapse of capitalism and, hence, providing a historical mandate for a fundamental reorganization of the political-economic order (Thum 1982: 18-9). This view

was not limited to the labor movement and was shared widely in Germany during the early post-war years. Indeed, even the Christian Democrats' founding party manifesto, the so-called Ahlener Program, stated explicitly that 'the capitalist system has failed the public and social interests of the German people. Following the terrible political, economic and social collapse as a consequence of a criminal power-directed politics, only a fundamentally new order can lead to a successful beginning.'¹²⁶ (Kunz et al. 1975: 127). In short, the belief that the instabilities generated by unfettered capitalism and funding by big industrialists brought the Nazis into power were widespread at that time (see also Markovits 1986: 66-67).

Economic democracy and socialization of key industries were the core components of the economic reorganization that the labor unions envisaged (Bunn 1958: 283; Schmidt 1977: 53-96). Socialization and economic democracy should serve the de-Nazification of the German economy. The industries to be socialized were those that had been particularly tarnished by cooperating with the Nazis, notably the iron and steel industry, coal mining and chemicals (Markovits 1986: 66). The goal was to deprive the allegedly antidemocratic heavy industrialists of their power and to give labor 'the utmost influence' over all aspects of the economy, as the future DGB president Hans Böckler said in 1946 (Müller 1991: 127).

The Allies considered the labor movement as the representative of a dormant democratic tradition in Germany and were, generally speaking, sympathetic towards its demands. On the issue of how to reorganize the ownership structure in the heavy industry, however, they disagreed. The UK supported socialization, while France and the US were opposed. In the end, the Allied High Council decided in November 1948 that the decision over the ownership structure of the heavy industry should be delegated to a future German government (Markovits 1986: 77; Van Hook 2004: 251-4). In the first national elections, in 1949, the Social Democrats were running on a platform that included socialization and economic democracy, while the Christian Democrats advocated the social market economy and free market competition. As shown in chapter 7, its advocates understood the social market economy as an alternative to economic planning and socialization. The coming into power of a non-socialist coalition government in 1949 undid the prospects for a socialization of the heavy industry. Though the SPD and the DGB still continued advocating socialization for some years, in reality these plans were now off the political agenda and the labor movement shifted its focus to codetermination, instead (Thum 1982: 146-9; Van Hook 2004: 257).

¹²⁶ The CDU did return to a pro-capitalist platform shortly after, however.

The political rehabilitation of German industry after the early de-Nazification period and its regaining of political strength encouraged industrial employers to go on the offensive against codetermination. Employers of all sectors opposed codetermination and propagated weaker forms of employee participation. Business opposition to codetermination was articulated primarily by the two peak-level federations, the Federation of German Industry (BDI) and the Confederation of German Employer Associations (BDA). The reasons for employers to oppose codetermination mirrored the reasons for unions to support it. All arguments used by employers against codetermination started from the assumption that codetermination was intended by the unions as a means for the socialization of ownership (Bunn 1958: 284). As the epigraph to this chapter illustrates, employers viewed codetermination as part of a piecemeal strategy by unions to socialize ownership by indirect means. It was precisely this incrementalist character of economic democracy that alarmed employers, because it appeared as politically much more viable than the revolutionary slogans of the radical left (Borsdorf 1987: 22). Employers understood codetermination not as a tool for the integration of the working class into a capitalist system, but as tool to overthrow capitalism.¹²⁷

Employers did not generally oppose employee participation rights, but wanted to see them limited to issues of social policy and working conditions and to the level of the workplace, rather than to the level of the entire firm. Employers did not reject employee participation rights at the workplace level concerning issues like working time and vacation arrangements, safety regulations, occupational social benefits, and the like¹²⁸ (Bunn 1958: 289). However, codetermination rights for labor at the firm level on the basis of parity with capital were fiercely opposed by employers. Employers' opposition focused on the following three components of the codetermination demands by unions:

- *parity representation*: unions demanded equal representation of workers and capital owners on the supervisory boards of all large companies. Employers opposed this decisive shift in the balance of power within firms to labor. Parity representation would mean a creeping expropriation of industrial ownership by restraining the discretion of capital owners over the use of their property.
- *union power*: unions demanded the right to appoint at least some of the labor representatives in the supervisory boards. Employers rejected any form of union

¹²⁷ The following paragraphs draw in particular on Bunn 1958.

¹²⁸ These rights had already been granted to labor in the Works Councils Law of 1920. Employers had originally rejected mandatory works councils as a potential vehicle for the aggravation of class conflicts, but in the meantime had come to accept them (see also chapter 4).

influence in the appointment of the labor representatives. Labor representatives should be appointed exclusively by the workforce of the firm, and not by external unions. Employers thus suspected a strengthening of union power as a result of codetermination.

- the *scope* of codetermination: unions demanded the right to codetermination on all aspects of firm policy. In contrast, employers wanted to limit the participation of labor representatives to social policy issues and exclude labor from decisions about broader economic issues, such as decisions over investments, production, or sales policy. Employers opposed the extension of employee participation from social policy to economic policy.

Employers justified their opposition to these three elements of codetermination by arguing that they would be fundamentally incompatible with the rights of capital owners. The right of private property includes the right of the owner to dispose of his property as he sees fit. Under codetermination, capital owners would however no longer be able to dispose over their property freely, as they would need to share this right with the representatives of labor. Therefore, although formal property titles remain unaffected, the rights flowing from this titles are severely curtailed by codetermination (BDA 1953b: 268; Bunn 1958: 290). On the basis of this argument, employers argued that codetermination would be a reformist way of establishing socialism. BDA president Walter Raymond declared in a speech in 1952:

The advocates of economic democracy seek, in the last analysis, the same goal as do the Marxists, upon whom the former rely. They also use as their point of departure, as did Marx, the allegation of the intolerable exploitation of the workers by capital.

But in contrast to Marx they do not want to achieve the immediate freeing of the working class through the risky method of “expropriating the expropriators”, that is, through socialization, but the end goal of socialism is to be preceded by the unobtrusive and safe method of penetrating the economy by means of codetermination (speech by Raymond, reprinted in BDA 1953b: 247-8).

Moreover, employers argued that codetermination would give unions excessive control over the economy. Employers suspected that the unions and their federation would be able to centrally control the labor representatives in the individual firms, and thereby would be able to use codetermination as a tool of centrally guided economic planning. The individual industrialist would be much weaker than the centrally coordinated labor representatives in the supervisory board of his firm. The unions would be aiming at replacing industrial leadership with its own people in order to gain full control over the economy, as the BDI stated in 1953:

The principal opponent of the entrepreneurial economy remains Socialism, even if it operates with slogans such as 'market economy of the left'. What it sticks to, however, is its demand to replace the elites. It intends to intensify the infiltration of leading positions in the administration and the economy with....affiliated intellectuals. The two co-determination laws have given a special impetus to this process. (BDI 1953: 28, translation by TP)

The sticking point in the conflict was thus whether control over the decision-making in firms should remain in the hands of capital owners or be shared equally with the representatives of labor. For employers this question appeared as a matter of capitalism versus socialism. Unlike social insurance in the 1880s (see chapter 3), employers did not see codetermination as an appropriate tool for pacifying the working class. Employers' position was also not motivated by potential effects of codetermination on labor productivity, labor loyalty and industrial peace. Such effects turned out as highly relevant in reality (see e.g. Streeck and Kluge 1999), but were not expected by employers at the time codetermination was introduced. The overwhelming fear of losing control over their firms and of a dramatic shift in the balance of power to the union side did not allow such considerations to develop during that time. Despite the massive resistance by employers, unions managed to achieve a partial success. The unions managed to institutionalize parity codetermination in the heavy industry. A diluted form of codetermination, acceptable also to employers, was instituted in large firms outside of the heavy industry. The next section looks at why employers did not succeed in preventing the introduction of codetermination, despite the resistance they put up.

8.II How Codetermination came about: The Policy-Making Process

The outcome of the codetermination conflict was a partial success for the labor movement. The labor movement did not manage to achieve its more far-reaching goals, socializing key industries and introducing economic planning, but managed to institutionalize parity codetermination in the heavy industry and a diluted form of codetermination in firms outside the heavy industry. The political conflict about the institutional principles of the political-economic order, which underpinned the codetermination conflict, was fought out in the context of the Allied occupation. The situation was characterized by a high level of uncertainty about the political and economic future of Germany. The labor movement perceived this situation as a window of opportunity for a thoroughgoing reorganization of the German economy, but it had to confront massive resistance from employers and their parliamentary allies. The introduction of codetermination was made possible through the cooperation of Allied occupation authorities. This section traces the processes that led to the

institutionalization of codetermination in order to show why business failed to fully prevent codetermination.¹²⁹

The introduction of codetermination in the heavy industry (1946/48)

Union demands for a reorganization of the economy, with a greater role for themselves, initially received a strong boost from the Allies' plans for reorganizing the German economy. While the Allies did not advocate codetermination as an institution, they needed the unions' cooperation in their own plans for reorganizing the German economy. At their conferences in Yalta and Potsdam the Allies agreed to destroy the concentration of economic power that characterized German industry and banking, and that had facilitated the waging of the war, by dismantling the existing cartelistic and oligopolistic structures. (Herrigel 2004: 363-76; Thum 1982: 26-31; Van Hook 2004: 250-3). In particular, the large combines in the heavy industry should be dismantled by splitting them into smaller independent units with new owners. These large combines often united mining, steel production and steel processing within one group. In 1938, 73 per cent of the national production of pig iron came from only six firms (Pritzkolet 1953: 196). The British occupation authority confiscated the shares of the heavy industry firms in its occupation zone in August 1946 and decided to hold them in trust 'for the German people' until a permanent solution for the ownership question would be found (Böhme 1978: 123). The old owners, often tarnished by their collaboration with the Nazis, should be expropriated and new owners should be found.

The unions' ambitions were furthered by a split between Allies. The US favored private enterprise, while the UK initially favored the nationalization of the large heavy industry firms. Most of the German heavy industry was located in the British occupation zone, which meant that the UK was in charge of carrying out its reorganization. The recently elected Labor government in the UK advocated nationalization and economic planning also in its own country and was, generally speaking, sympathetic towards the German labor movement. In October 1946, British Foreign Minister Bevin declared in the House of Commons that the German heavy industry should be nationalized (Berghahn 1985: 207). The UK occupation authority established an own agency in charge of West German heavy industry, the *North German Iron and Steel Control* (NGISC). The NGISC held the confiscated iron and steel combines in trust and was in charge of carrying out the intended reorganization of the heavy industry (Thum 1982: 33).

¹²⁹ The following two subsections rely in particular on the detailed studies by Gloria Müller (1987), Eberhard Schmidt (1977) and Horst Thum (1982).

The NGISC played a crucial role in the introduction of codetermination. Although the NGISC officials held no ideological affinity for codetermination, their interest in union cooperation led them to make concessions to the latter. On October 15th, 1946 the NGISC got in touch with North German labor union leaders, seeking their expertise and support for the intended economic reorganization (Thum 1982: 33-4). The labor union delegation was headed by Hans Böckler, the future president of their national union federation (DGB). The labor unions had no real interest in the decartelization of the heavy industry, but were willing to cooperate with the NGISC if they could achieve stronger union control over industry in return. The cooperation was thus based on a strategic alliance.

The head of NGISC, William Harris-Burland, assured the union leaders that the firms would not be returned to their old owners and that ‘the interests of...the workers will be taken into consideration as far as possible’ (quoted in Schmidt 1977: 76). On December 14th, 1946 the NGISC presented detailed decartelization plans to the union leaders, which included also provisions for codetermination in the newly created firms. The NGISC offered that each decartelized firm would receive a supervisory board consisting of an equal number of representatives of labor and shareholders. The unions agreed in principle and the details of the plan were worked out between the two sides in the following weeks (Schmidt 1977: 77). The negotiations proceeded so fast that the appointment of supervisory board members was already discussed on January 7th, 1947 (Thum 1982: 34).

On the basis of this agreement, parity codetermination was introduced in 1947/48 in all iron and steel firms decartelized by the NGISC. These firms received a supervisory board consisting of five labor representatives and five capital representatives, plus a neutral 11th member appointed by the NGISC and acting as the chair. The labor representatives consisted of two members appointed by the works councils of the firm (one blue-collar and one white-collar representative), plus two members appointed by the labor unions, one by the national union federation (DGB) and the other by the metalworker union (IG Metall). The fifth labor representative was appointed jointly by the other four and was intended to represent the ‘public interest’. In addition, one of the three members of the firm’s executive board could only be appointed with the consent of the labor representatives in the supervisory board. This so-called “labor director” was in charge of the firm’s personnel and social policy affairs and enjoyed the same status as the two other members of the executive board. This model became the basis for the *Montan Codetermination Law*, the special law for the heavy industry passed by the national parliament in April 1951, which is discussed in the next subsection (Thum 1982: 36).

For strategic reasons, heavy industry responded with its own codetermination offer to unions. Employers were excluded from the negotiations between NGISC and the unions. The affected firms and their management did thus basically have no influence on what the two sides agreed upon. A group of managers from several major heavy industry firms approached the union leaders with an alternative proposal for codetermination in order to win the unions over to their side and to oppose decartelization (Potthoff 1986 [1957]: 42-6; Müller 1987: 142-3). Moreover, these employers also understood codetermination as an appeasement measure to weaken radical elements within the labor movement (Berghahn 1985: 211). The unions did not, however, respond to this offer because they thought they might be able to achieve a better deal by negotiating with the NGISC (Berghahn 1985: 211-215; Teuteberg 1981: 50-51).

This offer by the iron and steel employers did not reflect a genuine preference for codetermination but was motivated by the intention to win the support of the unions against the decartelization plans by the Allies. This is evident from the fact that only three years later (1950/51) German industry vehemently resisted the legislative institutionalization of parity codetermination (see below). In 1946/47, however, heavy industry employers were ready to make far-reaching concessions to the unions, in order to gain their support against the Allied reorganization plans (Berghahn 1985: 215-6; Potthoff 1986 [1957]: 50). Their temporary endorsement of codetermination was a strategic move to try to prevent the reorganization of their firms.

The legislation of codetermination in the heavy industry (1950/51)

With the formation of the Federal Republic (FRG) in 1949 the prospects for a reorganization of the German economy in line with union demands deteriorated. The first national elections resulted in an unexpected victory for the Christian Democrats and a defeat for the SPD. The Christian Democrats gained 31 per cent of the vote, the SPD 29.2 per cent, FDP/DVP 11.9 per cent, KPD 5.7 per cent, the rest going to smaller non-socialist parties (Markovits 1986: 76). Together with the Free Democrats and several smaller parties, the Christian Democrats could form a non-socialist coalition government. This coalition was led by the CDU party chairperson Konrad Adenauer as the first Chancellor of the new republic. While the labor wing of the CDU had favored a Grand Coalition with the SPD, its business wing, the predominant wing within the party, had preferred a non-socialist coalition. As the SPD remained in opposition, the labor unions could not rely on the Social Democrats to implement their reform programme through the parliamentary process.

The issue of codetermination split the governing parties. A majority within the coalition opposed parity codetermination, in line with employers' preferences. The Free Democrats (FDP), dependent on financial support from big business, were strongly opposed to codetermination and so was the powerful business wing within the CDU/CSU. Codetermination was supported by the non-partisan union federation (DGB), the Social Democrats and the labor wing within the CDU/CSU. The Christian Democrats were thus divided about codetermination along class lines. The multi-class voter base of the Christian Democrats resulted in different positions on codetermination within the party. Codetermination was a goal as important to the CDU labor wing as it was to social democratic unions. While the business wing was the dominant wing within the CDU/CSU, the party needed to take into consideration the preferences of its labor wing as well (Markovits 1986: 79). This was one of several reasons why the government had a strong interest that a compromise about codetermination would be found, though important members of the government opposed codetermination, most notably its Minister of Economics, Ludwig Erhard.

A second reason was the legislation of codetermination laws at the state level. Several regional states (Hessen, Bremen, Baden-Württemberg) had introduced their own codetermination laws in 1948, though these laws were suspended by the US governor, Lucius Clay, who was generally skeptical of codetermination. When talks between employers and unions broke down in 1950 (see below), the new US governor, John McCloy, threatened to reinstate the state-level codetermination laws. The threat of regionally fragmented legislation is likely to have spurred government and employers to seek a compromise (Jacoby 2000: 76; Thum 1982: 39).

Chancellor Konrad Adenauer played an important role as a mediator in the institutionalization of codetermination, though he personally opposed codetermination (Thum 1982: 42). In his inauguration speech in September 1949, he had announced the government's intention to provide a legal framework for industrial relations (Thum 1982: 34). The government wanted to restore the old ownership relations in the heavy industry and return the confiscated shares to their old owners. The Allies made their approval dependent on the codetermination conflict being solved (Brück and Eichner 1974: 177). The government thus needed to try to find an arrangement with the labor unions. Moreover, Adenauer hoped that a compromise with the labor unions would help to secure social peace and political stability in this period of high uncertainty about the political and economic future of West Germany

(Thum 1982: 146-9). In addition, as mentioned above, Adenauer also needed to pay attention to the wishes of the CDU's labor wing, which supported codetermination.

Initially, though, Adenauer and the government took a backseat in the conflict over codetermination and urged capital and labor to find a compromise on their own. For domestic and foreign policy reasons the government could not afford to ignore the issue of codetermination. At the same time, however, the issue could have lead to a potential collapse of the government, as Adenauer had to fear that the labor wing of his party would collude with the opposition Social Democrats to push through a codetermination law in parliament against the position of a majority within the government. Adenauer thus initially tried to stay neutral and not to offend either side (Thum 1982: 40). The government hoped that the two sides would find a compromise on that issue on their own, thereby preventing the need for the government to intervene.

During the year 1950 several rounds of negotiations between employers and unions took place. These negotiations were characterized by stalemate and none of the meetings produced any results. The first round of talks took place in Hattenheim in January 1950. The talks were chaired by the president of the BDA, *Raymond*, and the president of the DGB, *Böckler*. Another round of talks took place in March, but failed again to produce any compromise solution. The intransigence of both sides blocked the way to a compromise. The unions wanted to have parity codetermination extended to all sectors. They did not want to accept any diluted form of codetermination, such as a minority representation of labor in supervisory boards. The employers fundamentally rejected parity codetermination. Hence, the two sides could not find common ground.

In April and May the government came under increasing pressure to act due to two events. First, as mentioned, US governor McCloy threatened to reinstate regional codetermination laws, because of the lack of progress at the national level. The imminent reinstatement of these regional laws put both, employers and government, under pressure to act in order to avoid a federalization of the codetermination issue (Thum 1982: 39). Second, the parliamentary faction of the CDU/CSU had come forward with its own codetermination bill, intended as a compromise. However, this bill did not have the government's approval and was opposed by employers (Thum 1982: 42-7). In short, employers had to fear the legislation of codetermination rights against their will.

In response to the increasing pressure, Adenauer took the initiative and mandated his Minister of Labor, Anton Storch, to draft a bill for a codetermination law. Storch came from

the Christian Democratic labor movement and thus enjoyed the trust of the party's labor wing. The bill should fulfill the difficult task of accommodating both sides. This initiative was intended to pacify the labor wing within the CDU/CSU and avoid that the latter would vote with the Social Democrats in favor of a far-reaching codetermination bill. Such a bill would have dashed the hopes of employers and the government majority for a more limited codetermination law. A rift between the business wing of the CDU/CSU and the pro-business FDP, on the one side, and the labor wing of the CDU/CSU, on the other, would have risked the collapse of the fragile government (Thum 1982: 43-8).

The government presented its bill to the parliament in October 1950. In the meantime further talks between employers and unions in May and July had again failed to produce a rapprochement. The government bill gave labor only one third of the votes on the supervisory board, instead of full parity. The labor representatives would be elected by the works councils and had to come from the workforce of the firm. External union officials could not be appointed as labor representatives. The proposal thus excluded the unions from codetermination. Employers were willing to accept this proposal for a diluted form of codetermination, but the unions were not (Thum 1982: 46-7). Not only did the bill not extend parity codetermination to firms outside of iron and steel, as demanded by the unions, it also meant the dismantling of parity codetermination in the iron and steel industry, where it had already been introduced under the auspices of the Allies. The bill thus failed to pacify the labor movement, and had the contrary effect of alarming the unions that their goal of institutionalizing codetermination was now seriously at risk.

In the following months the conflict escalated. After the repeated failure of talks the unions had become disillusioned about the chances of achieving their goal by way of negotiations alone. As a result, both sides shifted their efforts to public campaigning and the mobilization of their constituencies. Most importantly, the unions announced a nationwide general strike for January 1951, if their demands were not met. The mining and metalworker unions (IG Bergbau, IG Metall) held strike ballots among their members. 96 per cent of the metal workers organized in IG Metall and 92 percent of the mine workers organized in IG Bergbau voted in favor of a general strike to insist on the legislation of parity codetermination (Berghahn 1985: 223-4; Brück and Eichner 1974: 176; Markovits 1986: 78). The strike threat was intended to put the government under pressure to stand up for the institutionalization of parity codetermination.

Employers also intensified public campaigning against codetermination. In November 1950, the BDI organized a rally in Cologne. The BDI was dominated by big industry and was

one of the main actors lobbying against codetermination. More so than the BDA, the BDI voiced the views of the hardliners within industry. At this rally, the BDI president Fritz Berg condemned calls for codetermination as an attempt to evoke an unfounded class antagonism:

‘Wherever it is claimed that there is a chasm between ourselves and our workers, it is a fiction that overlooks reality. Wherever one posits a deepening of an alleged chasm, one is practicing demagoguery. Whoever really tries to provoke a chasm, commits a crime.’ Speech by BDI president Fritz Berg at a rally in Cologne on Nov 8, 1950 (quoted in Van Hook 2004: 261)

Soon after the announcement of the strike threat the view took hold among employers and the government that a compromise with the unions needed to be sought. Employers and unions both called upon Adenauer to act as a mediator and to chair the negotiations (Thum 1982: 71-4). On December 19th, 1950 the BDA called for the negotiations to be restarted under the chairmanship of Adenauer. The ultimate goal of the negotiations should be to maintain social peace. Adenauer should try to convince the unions to moderate their position. The BDA urged the chancellor to ‘remind all involved parties which enormous danger Germany faces today and which devastating consequences a class confrontation would need to have’ (quoted in Thum 1982: 74). In a similar way, BDI president Berg also called upon Adenauer to try to influence the unions to moderate their position. The fact that the employers were calling on Adenauer to intervene and mediate in the conflict illustrates the dilemma faced by employers. They could have decided to continue to reject the unions’ demands at the price of provoking industrial conflict. Alternatively, they could have given in to the unions at the price of losing full control over their firms (Thum 1982: 74).

Adenauer accepted the call to chair the negotiations. He intended to prevent political polarization and destabilization, which potentially could have led to the collapse of his government. In January 1951 he held separate talks with employers and unions. Adenauer urged both sides to take more moderate positions. DGB president Hans Böckler however insisted that for the unions a weakened form of codetermination would not be acceptable, as this would be to the disadvantage of the workers in those firms where parity codetermination had already been introduced under Allied auspices (Thum 1982: 146-9). The government worked out a compromise proposal, which divided the issue into two domains. In iron and steel, codetermination shall be legislated on the basis of the NGISC model (parity representation), while a diluted form of codetermination would be established outside of iron and steel. The iron and steel industry should thus receive a separate arrangement, which would protect the gains the unions had already made in these sectors.

Employers were reluctant to accept this double arrangement, because they thought that this would set a problematic precedent that would allow the extension of parity codetermination to other sectors at a later date. Nevertheless, Adenauer managed to convince a majority of employer representatives to restart negotiations with the unions on the basis of this proposal. A minority of employer representatives remained stubbornly opposed to any compromise, among them the BDI president Berg (Thum 1982: 82). While the BDA welcomed the restart of the negotiations, the BDI opposed it. The final round of negotiations, chaired by Adenauer, involved five union representatives and five heavy industry representatives. The negotiating teams only included such representatives that had previously indicated to be willing to seek a compromise. Upon the Chancellor's request, the hardliners of the BDI accepted not to participate in this final round of negotiations (Thum 1982: 84).

The two peak-level federations, BDA and BDI, were trying to put pressure on Adenauer and the participating heavy industry representatives not to accept an overly generous compromise. While the negotiations were going on, BDA president Raymond wired a telegram to Adenauer urging him not to conclude any agreement that could have knock-on effects for the rest of the economy (Thum 1982: 85). In a similar way, BDI president Berg remarked with acrimony that the responsibility for any concessions made in the negotiations would rest with the government (Thum 1982: 82). He declared that:

the whole industry sees in these negotiations, which take place under the threat of a political strike, a fatal shock to the authority of the state and to the foundations of our still young democracy (Berg quoted in Berghahn 1985: 226, translated from German by TP).

Despite the intransigence of both sides, a compromise could eventually be found. This time, negotiations proceeded quickly, starting on January 19th and ending on January 25th. The compromise brokered by Adenauer followed the government's earlier proposal: Parity codetermination in the heavy industry shall be enshrined in law, but shall not be extended to the rest of the economy. Concerning the heavy industry, the compromise followed the model of the NGISC without changes: The supervisory boards of heavy industry firms should consist of an equal number of capital and labor representatives, plus a neutral chair. In addition, all codetermined firms should have a labor director dependent on the approval by the labor representatives. As a concession to the unions, parity codetermination was extended from iron and steel to include also coal mining, where it was not yet established.

Following this compromise, the German parliament passed two laws, a first one concerning codetermination in the heavy industry, the so-called *Montan Codetermination*

Law of 1951¹³⁰ and a second one for large firms outside of the heavy industry, the *Works Constitution Law* of 1952 (Monissen 1878: 68-72). The latter defines a much diluted form of codetermination (see below). In short, a compromise could be found by creating a separate arrangement for heavy industry that institutionalized the gains made by the unions under the political aegis of the UK. On January 29th, 1951 the DGB called off the planned national strike (Thum 1982: 86).

To sum up, the institutionalization of codetermination in the heavy industry was the combined result of strong mobilization by the labor unions, including the threat of a general strike, and the active efforts by Chancellor Adenauer to engineer a compromise between capital and labor. Together with their parliamentary allies, employers tried to prevent the institutionalization of parity codetermination. They succeeded only partially, because of Adenauer's decision to try to accommodate the labor unions. His behavior appears to have been motivated by a set of strategic considerations. Though Adenauer had very close links to the business wing of his party, he was concerned that the labor wing of his party would collude with the opposition SPD by presenting a joint codetermination bill in parliament. This would have undermined the stability of his coalition and could potentially have led to the collapse of the government.

Moreover, Adenauer wanted to gain the tacit acceptance of the labor unions for his foreign and economic policies, which involved, notably, the Western integration of Germany, the restoration of private capital ownership in the heavy industry and the free market policies of his Minister of Economics, Ludwig Erhard. These policies frustrated the unions' hopes for economic reorganization (Thum 1982). A further escalation of the conflict over codetermination, involving a general strike, could have endangered his foreign and economic policies and might potentially even have led to the collapse of his government. For this reason he decided to accommodate the unions with the issue of codetermination.

The 1952 Works Constitution Law

In contrast to the Montan Codetermination Law of 1951, the *Works Constitution Law* of 1952 turned out to be a huge disappointment for the labor movement. The Works Constitution Law regulated employee participation rights in firms outside heavy industry. The negotiations in January 1951 had left undecided how codetermination rights should be regulated in the rest of the economy. Still, the unions hoped to be able to extend parity codetermination to the rest of

¹³⁰ The full name of the law is 'Special Codetermination Law for the Iron, Steel and Coal Industries'. The law was passed on April 10th, 1951.

the economy through an incrementalist strategy. They hoped to extend codetermination by stages. The Works Constitution Law dashed these hopes. The law instituted a limited form of codetermination that was acceptable also to employers. The law was passed in July 1952 with the votes of the governing parties, while the SPD voted against (Teuteberg 1981: 62). The social democratic labor unions vehemently opposed the law and called it 'a dark moment for democratic development in the Federal Republic' (Markovits 1986: 81; Thelen 1991: 64).

The Works Constitution Law of 1952 consisted of two parts. The first part of the law regulated employee participation rights at the workplace level. The law reinstated the works councils, originally introduced by the Works Councils Law of 1920, but abolished by the Nazis. The new law defined the rights and responsibilities of the works councils in a somewhat more restrictive way than the Works Councils Law of 1920 (Thelen 1991: 74-5). The obligations of the works councils to serve the interests of the firm and to carry out their tasks in loyalty to the firm, already enshrined in the 1920 law, were strengthened. The Works Constitution Law obliged the works councils to 'work together with management in a spirit of mutual trust' (paragraph 2, part 1). The law included an explicit ban on works councils to initiate strikes and does not allow works councils to bargain over issues regulated by collective agreements (Thelen 1991: 76).

The second part of the law regulated codetermination rights at the firm level in large firms outside of heavy industry. Instead of extending parity codetermination to the rest of the economy, as the unions wanted, the law instituted a diluted form based on the proposal made earlier by the Christian Democratic Minister of Labor Storch. This form of codetermination was called 'one-third codetermination' (*'trittelparitätische Mitbestimmung'*) and applies to firms with more than 500 employees outside of the heavy industry. One-third codetermination means that labor is entitled to appoint one third of the members of the supervisory board, instead of one half. The remaining two thirds are appointed by the shareholders. Moreover, the labor representatives were not granted the right to veto the appointment of the labor director like in the heavy industry.

In addition, the Works Constitution Law differs from the Montan Codetermination Law with respect to the mode of election of the labor representatives. The Montan Codetermination Law gave the unions the right to appoint some of the labor representatives. Under the rules of the Works Constitution Law all labor representatives were elected by the workforce of the firm. Unions were not entitled to nominate candidates and could not veto appointments. Union representatives from outside the firm could be elected by the workforce,

but at least two representatives had to come from the workforce. Thus, the unions could exercise no control over the appointment of labor representatives.

The failure of the unions to extend parity codetermination to the rest of the economy was in part due to their failure to devise an effective mobilization strategy. The charismatic and popular president of the union federation, Hans Böckler, died unexpectedly on February 16, 1951 (Markovits 1986: 79). His death left the union federation without strong leadership and disoriented about the appropriate strategy for mobilizing against the Works Constitution Law. His successor, Christian Fette, was unable to provide strong leadership to the federation. Fette was voted out of office in September 1952, as a result of the disappointment among union members about their defeat (Markovits 1986: 81-82). After its defeat in the codetermination conflict, the officially non-partisan union federation moved closer to the SPD again. In the election campaign of 1953 the DGB openly supported the SPD by choosing the thinly veiled slogan 'vote for a better Bundestag' (Markovits 1986: 82).

In addition to a confused strategy of mobilization, the unions' failure to extend parity codetermination was also affected by the changing political climate. The onset of the Cold War and the surge in anti-communism in West Germany in the early 1950s had created an unfavorable political climate for the radical economic reforms advocated by the unions. Socialization and economic planning were far less palatable to the general public in 1952, compared to five years earlier, when parity codetermination was introduced in the heavy industry. At the same time, the political priorities of the Allies had changed with the onset of the Cold War. Thoroughgoing attempts to de-Nazify industry and politics during the early post-war years were now replaced by the priority to win West Germany as an ally in the confrontation with the Soviet Union and to secure the Western integration of the new Federal Republic. Related to this shift, the Allies lost interest in Germany's domestic social and economic policies and did thus not intervene in favor of the unions.

The issue of codetermination had been much more divisive than issues of welfare state formation and expansion. It is hardly possible to understand the divisiveness of codetermination without considering its embeddedness in the ideological controversy over the appropriate post-war political-economic order. Economic democracy and social market economy were the two polar concepts in this controversy. Unlike with social insurance, employers did not view codetermination as an appropriate instrument for consolidating the legitimacy of capitalism and for pacifying the working class. Instead, they viewed codetermination as an assault on the foundations of capitalism. Employers accepted social

insurance because they expected social protection to consolidate capitalism by helping to prevent radical alternatives. In contrast, codetermination did not represent such an alternative to a leftist challenge, but was perceived as part of that challenge. Codetermination was seen as an integral part of a wider union programme for socialisation and economic planning. The ideologically divisive nature of the issue made the development of lower-order preferences, the pursuit of second-best choices, difficult for both sides.

The introduction of parity codetermination in the heavy industry became possible because the industrialists were bypassed by the relevant actors. The collaboration of the UK occupation authority made the introduction of parity codetermination in the heavy industry possible. The discredited moral and political legitimacy of the heavy industry had allowed the two protagonists to exclude its representatives from the negotiations. Once this precedent was set, it turned out to be difficult to dismantle. The Christian Democratic-led government of Adenauer assisted in the institutionalization of parity codetermination by helping to forge a compromise between capital and labor. For several reasons the Adenauer government in its early period had a strong interest in accommodating the unions. In this very early period of the newly founded Federal Republic, characterized by high levels of uncertainty about its future development, the maintenance of social peace and political stability was a top priority for Adenauer. Under the threat of a national general strike, Adenauer decided to accommodate the labor unions and put employers under pressure to accept a compromise. While the government of Adenauer was, generally speaking, an employer-friendly government, manifest in the free market policies by its Minister of Economics Ludwig Erhard, on the issue of codetermination conflicting pressures prevented it from siding firmly with employers.

8. III Continued Confrontation: The Codetermination Reforms in the 1970s

The conflict over codetermination was far from settled after the reforms of the early 1950s. For the next three decades the unions tried to undo the 1952 defeat and extend parity codetermination to the whole of industry. Industrial employers, in turn, were committed to prevent such an extension.¹³¹ While employers and unions maintained their original positions, the arguments they marshaled in favor of their position changed substantially over time. Neither the fears of employers nor the hopes of unions had materialized with the practice of codetermination. Clearly, the introduction of parity codetermination in the late 1940s had led neither to the breakdown of the heavy industry nor did it herald the advent of a socialist

¹³¹ Some heavy industry firms (e.g. Mannesmann, Rheinstahl) tried to evade codetermination, for instance, by restructuring their firms or changing their legal form in such a way that they would not anymore be subject to the rules of the Montan Codetermination Law (Katzenstein 1987: 1309; Müller 1991: 269; Teuteberg 1981: 59).

planned economy in West Germany, as industrialists had suspected. The socialisation fears of employers had turned out as unfounded.

At the same time, the labor movement had changed its ideological orientation over time. During the 1950s the labor movement eventually abandoned its Marxist ideology and socialisation goals and instead came to accept the social market economy and free market competition as the organizing principles of West Germany's political-economic order. The last elements of Marxist theory and ideology were eliminated by the SPD in its Bad Godesberg platform (1959) and by the DGB in its Düsseldorf platform (1963) (Katzenstein 1987: 125; Höpner 2005). Socialisation was now no longer seen as a defining principle of socialism but merely as one of several means for controlling economic power (Berman 2006: 190). Nevertheless, although codetermination had now finally lost its original ideological justification as an intermediary step towards socialisation, the extension of codetermination remained a core demand of the labor movement. The unions now argued that codetermination would be an important complement to political democracy, a way "of mitigating as far as possible [the worker's] oppressive feeling of helplessness and dependence" (DGB 1966: 31-2). Despite these changes in its meaning, codetermination remained a highly contentious issue also over the following decades, as this section shows.

Employers' continued opposition to codetermination

After the unions reinvigorated their campaign for extending parity codetermination in the 1960s, employers focused their agenda on preventing its extension. In response to the union campaign, the BDA formed a committee on the issue of codetermination, made up of representatives of the BDA as well as the other peak-level business federations. The committee was headed by the future BDA president, Hans-Martin Schleyer. It had the mandate to develop a common response by the business federations to the union demands for the extension of codetermination. The establishment of such a committee shows how much importance employers attached to that issue. The committee issued a report in October 1965 (BDA 1965; Erdmann 1966b: 308-11). In short, the BDA argued that:

an extension of codetermination would increase trade unions' power and immediately raise the question of their role and functions in a free economy. It would also entail a fundamental change in our property structure and thereby endanger the very basis of our free socio-economic order and its future development.

German employers are, therefore, opposed to trade union demands for an extension of the codetermination system (Balke 1966: 3).

While employers continued their opposition to parity codetermination, they had now changed their arguments. As the labor unions had abandoned their socialisation goals, the original argument that codetermination would herald the transformation of the German economy to a socialist system had lost its credibility. Instead, employers now argued that codetermination would be an obstacle to effective business management. BDA president Siegfried Balke summarized this argument in a speech:

We did not think that the Supervisory Board lends itself to a composition of heterogeneous groups. Management of a company has to be responsible to the owners and it cannot be effective ... if important decisions can be subject to compromises between groups which have very different interests and, in some cases, even political concepts. (...) Modern and enlightened management of industry does not require trade union control and participation in management in order to strive for good and sound relations at the work place (Balke 1966: 10-1).

At the same time, the employer federation maintained its established argument that codetermination would lead to an excessive concentration of union power and thereby endanger the balance of power between the two sides that is necessary for a true social partnership to function properly:

The spreading of this system [parity codetermination, TP] over the entire economy would indeed mean creating a network of centrally steered trade union control over the entire economy, and thus constitute an amalgamation of power in the hands of the trade union movement which would be without precedent (Balke 1966: 13).

In addition, employers responded to the union demands by arguing that parity codetermination would offer no added value to employees compared to the weaker forms of employee participation enshrined in the Works Constitution Law of 1952. Employers over time began to cherish the Works Constitution Law with its weaker provisions as an alternative to full parity codetermination. In particular, employers began to embrace the works councils, which they came to see as an important institution for the improvement of communication between employer and workforce (Erdmann 1966a). Employers abandoned their objections to the works councils, which they held during the Weimar Republic, and began to praise them as an alternative to the extension of parity codetermination. In his speech against the extension of parity codetermination, Siegfried Balke emphasized:

The application of the [1952 Works Constitution] Act in general has stood its test. It has contributed much to better understanding of mutual problems of employers and workers, and thus promoted industrial peace at the work place. We as employers support this Act and shall do our best to assure its still better application (Balke 1966: 8).

The Biedenkopf Commission: taking stock of codetermination

As a response to the reinvigoration of the codetermination campaign by the unions, the Grand Coalition government, consisting of Christian Democrats and Social Democrats, established

an expert commission in 1967. The commission was chaired by the Christian Democratic politician *Kurt Biedenkopf*. This commission was mandated to take stock of the effects of codetermination and to make recommendations for possible modifications and extensions of codetermination. Expert commissions are sometimes used in Germany as a delaying device, when the government tries to avoid making a decision on an issue that appears as politically unwelcome. The Codetermination Commission did not submit its report before January 1970, after the change in government to a coalition between SPD and FDP.

The findings of the report by the *Biedenkopf Commission* in general tended to vindicate codetermination. The report argued that codetermination 'is not only politically requisite and historically appropriate but is a factual necessity' (Mitbestimmungskommission 1970). The report found that codetermination had improved the flow of communication and information within firms and had instituted compulsory cooperation and deliberation between employer and employees. The report also found that codetermination was not used by the unions as an instrument for implementing their own independent economic policy or for exercising centralized control over the economy. The suspicion that union headquarters would try to use codetermination as a tool to 'remote control' decision making by firms had been one of the arguments used by employers against codetermination, as shown above. The report thus generally tended to dismiss employer suspicions as unfounded or exaggerated (Mitbestimmungskommission 1970; Cullingford 1976: 68; Wood 1997).

Despite this generally positive assessment, the recommendations of the report fell short of endorsing the unions' demand for an extension of parity codetermination. The report recommended an increase in the number of labor representatives in firms subject to one-third codetermination, but, at the same time, the retention of a majority of owner representatives. The unions were disappointed by the report's recommendations. However, in a strategic move, the unions announced that they were prepared to accept the recommendations of the report as a first step towards the improvement of the 1952 Works Constitution Law. Parity codetermination would still remain their ultimate goal. At the same time, however, a proposal was circulated by the DGB in the national parliament that included its previous demands for full parity, possibly with the purpose of winning over the labor wing of the opposition Christian Democrats.

The 1972 reform: avoiding the codetermination issue

After the change in government in 1969, the union campaign for codetermination gained fresh impetus. The grand coalition by the CDU/CSU and the SPD had been replaced by a coalition between the SPD and the FDP. The CDU/CSU and the FDP opposed an extension of parity codetermination. Chancellor Ludwig Erhard (CDU) was a staunch opponent of codetermination and opposed its extension on 'legal, economic and political grounds' (quoted in Erdmann 1966b: 311). The change in government in 1969 shifted the balance of power in government in favor of the supporters of parity codetermination, as the SPD became now the dominant coalition partner. The labor unions had long pinned their hopes for an extension of parity codetermination on the SPD. The shift to a SPD-led government had thus raised the expectations of the labor unions. The new Chancellor Willy Brandt (SPD) was a strong supporter of codetermination. In his government declaration of 1973, Chancellor Brandt stated that 'Codetermination belongs to the substance of the process of the democratization of society' (government declaration on January 18th, 1973, quoted in Monissen 1878: 57.) The new government was thus expected to be much more susceptible to union demands than previous governments.

Like the previous government, the social-liberal government was internally split on the issue of codetermination. While the SPD supported parity codetermination, the pro-business Free Democrats (FDP) were adamantly opposed. In October 1970, the Minister for Labor and Social Affairs, Walter Arendt,¹³² presented a first draft for an amendment of the Works Constitution Law of 1952. The draft was based on the recommendations of the *Biedenkopf Commission* and recommended a relative increase in the number of labor representatives, but falling short of full parity. The draft encountered the staunch resistance from employers and the FDP. The FDP made clear that it would not accept an extension of parity codetermination. The Social Democrats were thus faced with a dilemma. They were confronted with strong pressure from the unions to extend parity codetermination, but at the same time wanted to prevent a collapse of the coalition with the pro-business FDP.

After six weeks of internal discussions behind closed doors, the government came up with a new bill for an amendment of the Works Constitution Law, which had the approval of the full cabinet. The law was passed with the votes of both governing parties and against the votes of the opposition CDU/ in January 1972 (Katzenstein 1987: 138). The revised bill had little resemblance with the previous one and merely extended works council competencies, while not touching on the issue of codetermination at the firm level. Works councils received

¹³² Before becoming minister, Arendt had been head of the German Mineworkers' Union.

additional rights to information and consultation on a number of issues, including hiring and firing and workplace design. The codetermination component of the 1952 Works Constitution Law remained however unchanged (Jürgensen 1981: 75; Peltzer 1972: 11-9). The unions were disappointed and decided to continue their campaign for the extension of parity codetermination.

The 1976 Codetermination Law

The following years were characterized by a protracted debate between the two coalition partners. The two governing parties, SPD and FDP, both gained strength in the 1972 elections and decided to continue their coalition. Like his predecessor Willy Brandt, also the new Chancellor Helmut Schmidt was a strong supporter of codetermination (Schmidt 1976). In response to strong union pressure, the SPD made a renewed effort to convince its smaller coalition partner that an extension of codetermination was unavoidable. After several years of debate and several drafts and proposals, the two coalition partners finally agreed on a compromise in 1976. The bill was passed by parliament in April 1976, with the support of not only the governing parties but also the opposition CDU/CSU (Katzenstein 1987: 138).

The compromise was characterized by the concessions made by the SPD to the FDP. The SPD accepted to abandon the goal of full parity codetermination by accepting an arrangement called ‘under-parity codetermination’ (“*unterparitätische Mitbestimmung*”). This arrangement was defined as follows: In all firms with more than 2000 employees not subject to the Montan Codetermination Law, labor and capital appoint an equal number of representatives to the supervisory board.¹³³ The principle of parity representation is, however, impaired by two important qualifications, thus the term ‘under-parity’. The first concerns the role of the chairperson. The chairperson is elected by a two thirds majority from among the supervisory board members. If no two thirds majority can be achieved, the capital representatives elect the chairperson. In effect, this means that the chairperson is generally appointed by the capital representatives. More importantly, the chairperson has the right to cast two votes, if necessary to break a tie. The Codetermination Law of 1976 thus in effect secures a majority of votes for the capital representatives, though only a narrow one (Jürgensen 1981: 77; Schweitzer 1984: 275-6).

The second qualification concerns the role of managerial staff in codetermination. The labor representatives had to include a certain number of representatives of the managerial

¹³³ In firms with less than 10,000 employees, the supervisory board consists of 12 members, 6 representing labor and the other six capital. In larger firms, the supervisory board is enlarged.

staff, the so-called ‘senior white-collar employees’ (“leitende Angestellte”). The unions perceived this rule as undermining the parity principle, because the managerial representatives are likely to side with capital owners rather than with workers. This rule thus makes it more difficult for labor to form a uniform group. Blue-collar and white-collar employees elect their representatives in separate elections, whereby the number of representatives for each group is proportionate to its share of the workforce.¹³⁴ The complex system of quotas for these three occupational groups; blue-collar employees, white-collar employees and senior white-collar employees; tends to produce an over-representation of the managerial employees in the supervisory board (Monissen 1878: 74-76, see also; Cullingford 1976).

In short, the Codetermination Law of 1976 reflects a compromise between the two governing parties, SPD and FDP. Chancellor Helmut Schmidt and his SPD were faced with a dilemma. Schmidt was a supporter of codetermination (Schmidt 1976) and wanted to reward the labor unions for their tolerance of the government’s austerity programme and their wage moderation. The SPD’s junior partner, the FDP, however, was adamantly opposed to an extension of parity codetermination, which foiled the attainment of full parity codetermination. The result did not meet the expectations of the labor unions, which declared their intention to continue to strive for the extension of full parity codetermination to all sectors.

Employers challenge codetermination in court

The Codetermination Law of 1976 did not satisfy employers either. For the unions the law did not go far enough, for employers, in contrast, it went much too far. Despite its qualifications on parity representation, employers rejected the law. They questioned the constitutionality of the law by filing a constitutional complaint to the Federal Constitutional Court in 1977.¹³⁵ Employers argued that the Codetermination Law of 1976 violates the constitutional rights of private property ownership. In 1979, the court decided to reject the complaint and confirmed the constitutionality of the Codetermination Law. The court based its decision on the argument that the constitution “does not prescribe or guarantee a particular economic order” and instead ‘leaves ordering the economy to the legislature’ Wiedemann, 1980 #2455: 90}. The BDA accused the labor unions of having put illegitimate pressure on the court, but nevertheless accepted the court’s decision (BDA 1979: XV-XIX).

¹³⁴ External union representatives can be appointed if elected by the workforce. The unions have no right to appoint labor representatives, in contrast to the Montan Codetermination Law.

¹³⁵ The lawsuit to the Federal Constitutional Court was filed by 29 employer associations and nine individual firms (Wiedemann 1980)

The employers' resort to the Constitutional Court was part of a wider offensive by employers against what they perceived as an excessive concentration of union power. In March 1974 the employer federation (BDA) started its so-called 'union state' campaign, which was intended to shift public opinion against the labor unions. As Andrei Markovits has put it: 'Under the motto "market economy or union state," the employers initiated a massive attack designed to sway public opinion against the unions, who - in the employers' view - were beginning to dominate the country and threaten the very fabric of liberal democracy' (Markovits 1986: 125). The BDA argued that the unions had undergone an ideological radicalization since the early 1970s, which would jeopardize the foundations of the social market economy. Moreover, the BDA targeted its attack against the 'entanglement' ("Verfälschung") of the unions with the SPD, which, in their view, threatened to lead to a so-called 'union state' (Markovits 1986: 138). These concerns about an excessive concentration of power in the hands of the unions were certainly not new and had already played an important role in the codetermination conflict in the early 1950s. With the resurfacing of the codetermination conflict in the early 1970s, however, these arguments gained new momentum.

The deterioration of relations between capital and labor in the second half of the 1970s is not only reflected in the employers' public campaigning against the 'union state' and their resort to the Constitutional Court, but also in an intensification of industrial conflicts. An intensified use of lockouts and strikes characterized the second half of the 1970s (Markovits 1986: 142). As the unions supported locked-out workers, the intensified use of lock-outs by employers constituted a heavy burden on union finances. Moreover, the BDA had undergone an organizational restructuring during the 1970s, under its new leader, Hans Martin Schleyer. Schleyer transformed the previously weak umbrella federation into a centralized and well-coordinated organization, which coordinates the strategies of its member associations in bargaining with unions. Characteristic of this new-gained strength of the BDA was the intensified use of the so-called 'taboo catalogue' by the federation, an enumeration of issues on which member associations were not allowed to make concessions to unions (Schroeder 2000: 175-8; Thelen 1991: 119-20). The conflict over codetermination had contributed considerably to this deterioration of industrial relations in the 1970s.

SUMMARY: ARGUMENTS USED BY THE BDA AGAINST PARITY AND UNDER-PARITY CODETERMINATION

- obstructs the effective functioning of enterprises in a market economy
- is fundamentally incompatible with the economic system of a market economy
- parity representation means, in fact, an over-representation of labor ('over parity')
- involves a risk of stalemate situations and, as a result, problematic concession bargaining
- parity in the supervisory boards may induce parity in the executive boards
- parity codetermination means more influence for the unions (concentration of power in the hands of the unions)
- undermines wage bargaining autonomy, by making employers and their associations dependent on union support
- undermines the balance of power between the social partners
- curtails ownership rights (restricts owners' disposition over private property)

Source: BDA Annual Report 1974 (1974: 160-162).the list summarizes the arguments listed in the BDA opinion in response to the 1974 government bill for a new Codetermination Law.

8. IV Codetermination Today

Despite their massive resistance German industrialists could not prevent codetermination becoming a permanent and stable component of the German system of industrial relations. The past struggles between capital and labor have resulted in a fragmented system, consisting of three different types of codetermination (see table 8.2 below): full parity codetermination (Montan Codetermination Law of 1951), under-parity codetermination (Codetermination Law of 1976) and one-third codetermination (Works Constitution Law of 1952). Full parity codetermination has lost importance over time due to the structural decline of heavy industry (Parnell 1994). Hence, the under-parity variant (firms with more than 2000 employees) and one-third variant (between 500 and 2000 employees) are the most widespread variants of codetermination today.¹³⁶

¹³⁶ The development of the institutional basis of codetermination since the 1976 reform has been characterized by incremental adjustments. Among other things, election rules have been simplified and rules have been extended to new legal types of firms (Kommission zur Modernisierung der deutschen Unternehmensmitbestimmung 2006: 81-4).

Table 8.1 Existing Variants of Codetermination in Germany

Year	Law	Applies to	Workers covered (in % of all West German workers, late 1970s)
1951	Montan Codetermination Law (full parity codetermination)	Firms in coal mining and iron and steel production with more than 1000 employees	2.6
1952 (amended 1972)	Works council component of the Works Constitution Law (only works councils, no codetermination)	All firms with at least 5 and less than 500 employees	44.8
1952 (amended 1972)	Codetermination component of the Works Constitution Law (works councils + one third codetermination)	Firms with at least 500 and less than 2,000 workers not subject to Montan Codetermination	4.3
1955	Civil Servants Personnel Representation Law	Public employees, incl. railroad and postal workers	14.8
1976	Codetermination Law (under-parity codetermination)	Firms with more than 2000 employees not subject to Montan Codetermination	19.6
-	Not subject to Works Constitution Law	Small firms (<5 employees)	13.9
-	-	All Firms	100

Source: Niedenhoff 1979: 20 . Percentage of employees refers to the late 1970s

Despite the staunch opposition by employers against the introduction and extension of codetermination, in practice of codetermination in German firms has turned out as largely cooperative. Codetermination has not turned out as an intermediary step towards the socialisation of industrial ownership, neither has it turned out as a tool for centralized economic planning in the hands of the unions. Instead, codetermination has developed into a pragmatic tool of employee participation in firm decision-making. Codetermination has not

led to a reorientation of business policies, away from pursuing pure profit motives to pursuing wider social goals, as the protagonists of economic democracy in the 1950s expected. Instead, the labor unions had come to accept that codetermination operates within the constraints of a market economy. They have come to understand codetermination as a goal in itself, rather than as a means towards socialism. In reality, the labor representatives see themselves as the representatives of the economic interests of the firm's workforce, rather than of the interests of the working class at large or as protagonists of some wider social movement or common good. In short, it appears that the practice of codetermination has made labor more pragmatic.

At the same time, German firms have, by and large, managed to come to terms with codetermination. Academic studies find that codetermination tends to have positive effects on productivity and competitiveness or does, at least, not have negative effects (e.g. Vitols 2005). In particular, codetermination has facilitated workforce restructuring and labor shedding in sectors undergoing structural decline, like coal mining (Parnell 1994). Employee representatives and management have negotiated innovative forms of personnel management that has facilitated the economic restructuring in these sectors, including early retirement schemes, retraining schemes, part-time work or flexible working time (Jackson 2005: 246-9).

Reports of several expert commissions have emphasized the positive economic effects of codetermination. For instance, the German federal government has recently mandated a commission to evaluate the economic effects of codetermination and make recommendations for a potential reform. Reviewing the econometric literature on this topic, the participating experts concluded cautiously that there is no evidence of any negative impact of codetermination on the profitability or productivity of codetermined firms, while there may potentially be positive effects (Kommission zur Modernisierung der deutschen Unternehmensmitbestimmung 2006: 14). A report by another expert commission in 1998, organized by the private think-tank *Bertelsmann Foundation*, emphasized the positive effects of codetermination on economic efficiency (Streeck and Kluge 1999; Bertelsmann Stiftung and Hans-Böckler-Stiftung 1998).

In his analysis of the economic consequences of codetermination, Wolfgang Streeck has argued that codetermination has functioned as a '*productive constraint*' on firms (Streeck 1992). Firms have adjusted their production strategies to codetermination and have developed production strategies that benefit from codetermination. In particular, production strategies focusing on product diversification and product quality ('diversified quality production') have benefited from codetermination (Streeck and Kluge 1999: 12-15). According to Streeck, firms have changed the way they utilize labor in response to codetermination. Labor representatives

have partially taken over managerial responsibilities, which reinforced their interest in cooperation with management (Streeck 1992: 137). In effect, codetermination has, thus, made capital and labor more alike. Capital has internalized the interests of labor, while labor has internalized the interests of capital (Streeck and Kluge 1999; Streeck 1992).

The official position of German employers towards codetermination stands in marked contrast to the findings of these studies. Even today, German employer associations, officially and publicly, oppose parity codetermination. Even though negative statements by individual managers or entrepreneurs are rare, the two top federations still call for the abolition of (under-) parity codetermination. In a joint press release in November 2006, for instance, the presidents of the BDA and the BDI, Dieter Hundt and Jürgen R. Thumann, declared that: ‘A large number of firms ... see codetermination as a competitive disadvantage for Germany’ (BDI and BDA 2006: 1). These competitive disadvantages are:

Decisions over investments are slowed down [by codetermination]. In cross-border mergers...codetermination is often seen as an obstacle by the firms involved...In comparison, the one-third codetermination of employees in the supervisory boards enjoys a significantly greater acceptance among the firms (BDI and BDA 2006: 1, own translation).

There has thus been remarkable continuity in the official positions of German business associations since the 1950s, despite the apparently positive experiences with codetermination in many firms. Then and now, employers consistently opposed (under-) parity codetermination and advocated one-third codetermination and works councils as more acceptable and beneficial alternatives of employee participation. These alternatives are just as well able to provide the merits of employee participation, such as improving the flow of intra-firm communication, securing social peace and improving employee motivation and productivity, while at the same time maintaining capitals’ ultimate authority over decision-making in the firm. In the same press release, BDA and BDI demand that under-parity codetermination be dismantled and replaced by one-third codetermination:

One third codetermination of the employees in the supervisory board provides the right measure for making the optimal use out of the acknowledged advantages of codetermination. One third codetermination is also the most widespread form of codetermination in Europe (BDI and BDA 2006: 1, own translation).

In a similar way, as early as 1966 BDA president Balke promoted one-third codetermination as an alternative to parity codetermination:

We consider it an indispensable principle that management is appointed by and responsible to the owners of the company. As long as two-thirds of the members of the Supervisory Board are actually representatives of the shareholders, this principle can be considered maintained (Balke 1966).

While employers consistently maintained their opposition to parity codetermination from the early 1950s to today, the arguments they marshaled to back their position changed in remarkable ways over time. During the 1950s employers branded codetermination as a threat to the social market economy, as a disguised form of socialisation and a tool for union-controlled economic planning, violating the private property rights that West German society would rest upon. When the fears of socialisation and economic planning waned due to political developments, employers in the 1960s and 1970s shifted their lines of argument. They now argued that codetermination created excessive union power, threatened the balance of power that social partnership was based upon and constituted an obstacle to effective business management, given the imperatives of a market economy. Today, they argue that codetermination is incompatible with the competitiveness requirements created by the internationalization of financial markets. Codetermination constitutes a competitive disadvantage for German firms in their competition for international investment capital (statement by the employer representatives in *Kommission zur Modernisierung der deutschen Unternehmensmitbestimmung* 2006:56-8). In short, while the arguments have changed, the positions tend to remain the same.

The new interpretation of codetermination as a competitive disadvantage for German firms reflects the turn of many German firms to shareholder values since the 1990s. This new shareholder value-orientation is the result of changes in capital markets and corporate governance that have intensified the competition for international investors. This development involved a whole range of changes: the liberalization of domestic and international capital markets, the loosening of traditional bank ties and inter-locking ownership relations, the growing importance of new institutional investors and equity-based finance, stock options for management and reforms of corporate governance rules that have strengthened shareholder rights (Jackson 2005: 246-7). Codetermination is today seen by employers as an obstacle to an effective shareholder value orientation. The shift to shareholder values has shortened time horizons and raised profitability benchmarks. Codetermination slows down decision-making and requires concessions to labor that are seen as incompatible with shareholder values. Codetermination is therefore seen by industry as a disadvantage in competing for international investors (*Kommission zur Modernisierung der deutschen Unternehmensmitbestimmung* 2006: 57-8).

Conclusions

The case of codetermination constitutes a deviation from the politics of accommodation. In the social policy field employers have often endorsed specific policy options as lesser evils. In regard to codetermination the scope for accommodation was more limited due to the ideologically loaded nature of the conflict. Employers endorsed one-third codetermination and works councils as lesser evils compared to full parity codetermination, the goal of the labor movement. Nevertheless, the scope for a strategy of accommodating and pacifying the labor movement was much more limited in the case of codetermination, because German industrialists considered codetermination an infringement of essential property rights. They viewed codetermination as a Trojan horse, as part of a piecemeal strategy by labor to socialize industrial ownership. According to industry, codetermination would in effect expropriate capital owners, by shifting control over firm decision-making partly to labor. Codetermination did thus not offer itself as a concession to pacify a radicalized or discontent working class, because defending private capital ownership and entrepreneurial freedom were precisely the reasons why employers wanted to pacify the working class. Parity codetermination was not a suitable means to that end.

The case of codetermination testifies to the primacy of political interests over economic interests. Employers formed their preferences about codetermination on the basis of how they thought it would change the balance of power between capital and labor and how it would curtail their control over the use of capital. As the chapter has shown they did not form their preferences on the basis of considerations of how codetermination might support or undermine the kind of production strategies they intended to pursue. Arguments relating to labor productivity, worker motivation or the improvement of communication between management and workforce played little role in the conflicts over parity codetermination in the post-war period, neither for the unions nor for employers.¹³⁷

Employers understood parity codetermination primarily from the perspective of how it might curtail entrepreneurial control and boost union power. Even after the labor unions had abandoned their more radical goals for economic reorganization, to which codetermination was linked to, did employers continue to oppose codetermination as fundamentally incompatible with the principles of a free market economy (see table 8.1). This confirms the proposition that in the formation of employer policy preferences, political interests take

¹³⁷ Such arguments did play a role in employers' assessment of the works councils, though, which they came to cherish over time, but they did not shape employers' perspective on the issue of parity codetermination.

priority over economic interests. Conflicts over the distribution of power and control over investment decisions obstructed the view on the potential economic efficiency effects of codetermination. Despite the positive effects on competitiveness that academic studies attribute to codetermination, employers have not been a driving force behind its introduction and extension. The introduction and extension of codetermination in Germany has been characterized by class conflict, rather than class alliances.

9 Employers and the German Model Today

The consensus model is yesterday's model. Everywhere in the world people are recognizing that the principle of subsidiarity should also apply within the economy. In Eastern Germany firms are violating collective agreements everywhere. Without these violations the situation in the East would be even worse. I consider these violations not as disastrous, but as exemplary... In Germany we have too many Round Tables and too few quick and hard-edged decisions.

(Hans-Olaf Henkel, President of the *Federation of German Industry* [BDI] between 1994 and 2000. In *Der Spiegel* 01/1998: 72-74)

Although employers had not been a driving force in the development of the German model, as shown throughout this thesis, they did over time come to accept many of the policies and institutions that underpin this model. In particular during the post-war period, employers came to terms with political constraints, and, to some extent, discovered genuine advantages in policies and institutions whose introduction they had either opposed or endorsed only for strategic reasons. In particular, employers in the post-war period came to endorse two key institutions they had earlier on opposed or accepted only with reluctance: works councils and sectoral collective bargaining. Employers came to see institutions of social compromise as being better suited for securing social peace than the repressive means they had pursued during earlier times. In addition, they also developed a genuine interest in certain social policies that facilitated peaceful labor shedding by encouraging early exit from the labor market.

Since the 1990s, though, employers' support for institutions of social compromise gradually, but nevertheless decisively, eroded. Rather than relying on corporatist institutions of consensual policy-making, employers now turned to public campaigning to push for far-reaching reforms. They campaigned for systematic retrenchment of welfare state programmes, including early retirement, and labor market liberalization. At the same time, an erosion of collective bargaining institutions occurred as a result of primarily smaller firms abandoning them. These changes amount to a shift from a strategy of political accommodation, characteristic for the post-war period, to a strategy characterized by conflict and confrontation, rather than by compromise.

This chapter tries to provide an explanation for this shift in employers' political positions and strategies. Why did employers turn away from consensual policy-making and political accommodation? Why did they become protagonists of institutional change, rather than defending existing institutions against reform efforts? The explanation offered combines endogenous and exogenous developments. Domestically, the returns to social compromise declined as labor unions became more accommodationist over time, thereby reducing the efforts needed to sustain social peace. At the same time, the usage of social policies for the purpose of peaceful labor shedding resulted in ever-rising non-wage labor costs (see section 9.I below). As a result, reducing non-wage labor costs greatly gained in importance for employers. This new priority became increasingly difficult to reconcile with social compromise, given the existence of considerable political obstacles towards welfare retrenchment.

In terms of the exogenous context, the accelerating globalization of the economy during the 1990s made employers face stiffer cost competition, but also better opportunities for relocating investments abroad. As a result, employers became less dependent on domestic compromises, while at the same time these compromises had over time also become more costly. The combination of these two developments, I argue, motivated employers to turn away from social compromise and to push for far-reaching changes much more assertively than before.

This re-orientation in employer politics takes three forms. First, employer organizations began to campaign much more aggressively for cost-cutting reforms compared to previous periods, often risking conflicts with other actors. Through media statements and public campaigns they began to forcefully articulate an increasing dissatisfaction with existing policies and institutions and a desire for deregulatory reforms. They initiated and funded several public campaigns that focused on conveying an urgent need for political reforms to reduce labor costs and tax burdens in order to keep the German economy competitive. The so-called "Initiative New Social Market Economy" (INSM) constitutes the probably most forceful and prominent of these campaigns. Through public campaigning employers tried to circumvent the limits of corporatist policy-making, by shifting the political constraints created by electoral politics.

Second, employers' readiness to compromise and to accommodate labor demands declined over time. Efforts to reach corporatist compromises on welfare state and labor market reforms, such as the "Alliance for Jobs" talks, have been half-hearted and have essentially come to naught, due to the unwillingness of both sides to make concessions. Third,

and in addition to changes at the collective actor level, also individual firms have moved away from institutions of social compromise, by taking steps to either evade or exit collective bargaining institutions. Smaller firms and firms in East Germany, in particular, tended to abandon sectoral bargaining institutions. Other firms remained in sectoral bargaining, but did not comply with agreements. These reflect important developments that indicate that the readiness by German employers to pay the price for social compromise has eroded since the early 1990s. Tyll Necker, a former president of the *Federation of German Industry* (BDI), remarked that:

A point has been reached when a policy of compromise at any price can no longer be sustained. The decisive question is not “what will appease the unions” but “what will combat unemployment”...When necessary, one must be prepared for confrontation (Tyll Necker, former BDI president and, at that time, BDI vice-president, in *Die Zeit*, 22 March 1996).

The remaining sections of this chapter are structured as follows: after presenting the general argument briefly in the next section (I), the chapter turns to the empirical analysis. Section II analyzes the temporary return of cross-class consensus and social compromise in the wake of German unification. The subsequent sections analyze employers’ turn away from accommodation and compromise in the field of welfare state politics (III) and industrial relations (IV). The final section (V) discusses the factors explaining the changing politics of employer associations.

9.I Erosion of Social Compromise: Endogenous and Exogenous Factors

As shown in previous chapters, German employers often accommodated to political constraints, and have accepted compromise solutions. Political accommodation, i.e. the adjustment to political constraints, can be seen as a game of give and take. To what extent employers are likely to accommodate to political constraints depends on what they can expect to gain in return. Historically, political accommodation by employers was motivated by two goals: pacification and containment. Initially, the acceptance of the formation of welfare state policies and industrial relations institutions by employers was motivated by the goal of pacifying a potentially revolutionary working class. With the reformist transformation of the labor movement and the emergence of an affluent working class this goal subsequently became less relevant to employers.

The policies initially established as a means of social pacification had, however, in the meantime become a stable and well-entrenched element of the German political economy, and, with the democratization of the political system, could not be unilaterally dismantled by

employers, even if they would have wanted to. They needed to accommodate. As previous chapters have shown, employers' acceptance of welfare state expansion was neither the expression of an altruistic commitment, nor was it based on any economic self-interest in welfare state policies per se. Rather, it was based on the belief that political accommodation would be the most effective way of *containing* welfare state expansion. By cooperating with government policy-makers, business expected to be able to influence important details of planned policies with a view to containing the growth in non-wage labor costs. Political accommodation was aimed at containment of reform efforts within the limits of the politically feasible.

For several reasons, employers came to perceive this strategy as increasingly ineffective from about the early 1990s onwards. First, the rise in levels of social expenditure during the 1980s and 1990s, which employers wanted to stop, was not so much the result of deliberate government policy decisions, but, instead, resulted primarily from changes in socio-economic structures that led to a rise in benefit recipients. Higher levels of unemployment, demographic ageing and, most notably, the costs of reindustrialization in East Germany after unification were among the main factors behind rising social expenditures during this period (see sections 9.II and 9.III below). To counter this structurally induced rise in social expenditures required an active commitment by policy-makers to cost containment through benefit cutbacks. Employers had to try to promote such decisions.

At the same time, public opinion and electoral support for generous welfare state policies posed formidable obstacles towards any attempt of radical welfare state retrenchment. Like in other advanced industrialized countries, welfare state politics in Germany became shaped by the counter-veiling pressures of fiscal constraints on the one hand, and the electoral popularity of welfare state policies on the other, as Paul Pierson aptly pointed out (Pierson 2001: 411-9). Electoral competition between Christian Democrats and Social Democrats led both parties to appeal to the pro-welfare attitudes among large parts of the electorate and to be reluctant with implementing welfare state cutbacks. The 'new politics' of the welfare state, characterized by the goal of cost containment, came to follow a different logic than the previous politics of welfare state expansion, one in which the room for maneuver by policy-makers became more limited, due to the double constraints of electoral popularity and fiscal constraints.

In this context of the "new politics" of cost containment, employers now wanted not to contain reform efforts, as during the period of welfare state expansion, but to intensify them. In this changed context, trying to influence reform outcomes in employers' interest by

accommodating to the goals and power resources of relevant actors turned out as an increasingly ineffective strategy, because the room for maneuver of policy-makers themselves became more constrained. Electoral support for generous welfare state programmes was the main obstacle to the new politics of welfare state reform, an obstacle that was difficult to affect by way of accommodation. Unlike elite policy-makers, the electorate at large is unlikely to be responsive to statements by business representatives. Policy-makers are likely to listen to business proposals, because reforms that enjoy the acceptance of business appear more likely to be sustainable and promise higher levels of investments. During the period of welfare state expansion, trying to contain the ambitions of reformers by accommodating to their broader goals thus appeared as an effective strategy to employers. The shift from expansionary politics to cost containment meant that this strategy became less effective. Employers decided that they needed to take on public opinion, instead, if they wanted to achieve significant expenditure cuts.

At the same time, the accelerating of globalization in the 1990s amplified employers' unwillingness to acquiesce to existing domestic political constraints. Economic globalization, in terms of increasing trade and transnational capital flows, acts both as a constraint and as an opportunity for firms. Globalization intensified cost pressures on German firms, but also enhanced their opportunities to invest abroad and relocate production sites. According to one survey, conducted among German firms,¹³⁸ 60 per cent of respondents said that they faced "very severe" price competition and 34 per cent say the faced "severe" price competition (quoted in Kinderman 2005: 458). While German industry tends to rely on quality production, this does by no means exempt it from cost competition, as there are also many other countries that are able to compete in terms of quality. International competition does not, thus, take place exclusively in terms of quality or in terms of price, but in terms of a combination of both. Intensifying international cost competition and the simultaneous rise in domestic non-wage labor costs (see table 9.2 below) made political accommodation increasingly difficult to afford for employers.

At the same time, better opportunities to invest abroad or to even relocate production to other countries are likely to have contributed to making German firms more reluctant to accommodate to domestic political constraints. From the 1990s onwards, German employer organizations consistently relied on the exit threat to push their case for welfare state retrenchment. They systematically promoted the so-called *Standortdebatte*, the political

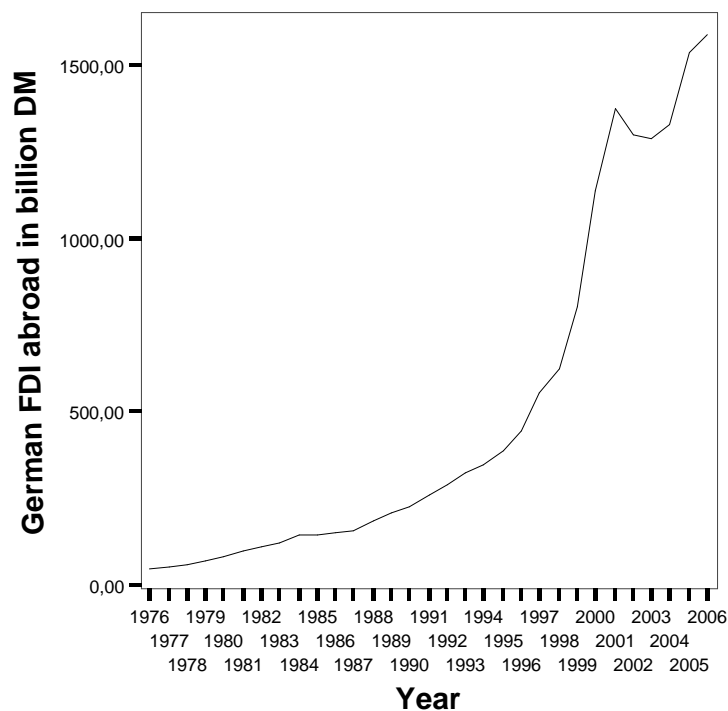
¹³⁸ The survey was conducted by the Institute for the German Economy (DIW), which is funded by employer associations (Gesamtmetall 2003).

debate over the need for policy reforms to improve the competitiveness of Germany as a location for investments (see section III). Employers used the threat of losses in jobs and investments to lower-cost countries to add authority to their demands for cost-cutting reforms.

The exit threat is not an empty threat. The assets held by German firms abroad (outward FDI stock) have multiplied in value since the early 1990s. The value of outward FDI equaled 8.7 per cent of GDP in 1991, and has since quadrupled to 34.9 per cent of GDP in 2006 (table 9.1 below). German firms have thus massively intensified their international investment activities. The international expansion of German firms is in reality not the mere product of high labor costs at home, but is also driven by other motivations, such as achieving closer proximity to relevant consumer markets (see e.g. Traxler et al. 2001). Nevertheless, the soaring of international investments has given credibility to the political use of exit threats and has, thereby, shifted the balance of power to employers. Moreover, investments abroad also made it easier for employers to compare labor costs and production conditions at home with that in other countries, and thereby are likely to have contributed to employers' increasing reluctance to accommodate to domestic political constraints. The international expansion of their activities has changed their geographical frame of reference, making them more reluctant to put up with domestic political constraints they had been ready to accept in the past.

To sum up, interacting domestic and international factors resulted in an erosion of employer support for institutions of social compromise and welfare state programmes. Domestically, the rewards to compromise in terms of securing social peace and influencing policy reforms declined. At the same time the costs of social peace went up. During the period of welfare state expansion, moderating their positions helped employers to more effectively influence reform output. During the new period of cost-containing reforms, strengthening, rather than limiting, reform ambitions became the new goal. At the same time, the internationalization of production and investments has reduced the dependence of firms on Germany as a production site, and, thereby, has also made them more reluctant to accommodate to domestic political constraints. Endogenously created problems, such as higher labor costs, met with a fiercer competitive environment. As a result, the costs of institutions of social compromise came to gradually outweigh the economic benefits they generate for firms.

Chart 9.1 German outward FDI stocks 1976 - 2006



Source: Deutsche Bundesbank (2008). Note: chart shows assets held by German firms abroad (outward FDI stocks), including both direct and indirect holdings (via foreign holding companies)

Table 9.1 German outward FDI in percentage of GDP 1991 - 2006

Year	1991	1993	1995	1997	1999	2001	2003	2006
% of GDP	8.7	9.6	10.6	14.8	20.4	33.0	30.4	34.9

Sources: Deutsche Bundesbank (2008) and Statistisches Bundesamt (2008), own calculations.

Employers: A force for stability or for change?

The argument of this chapter casts doubts on arguments that employer interests are a force for institutional stability. Many accounts of the development of the German political economy during the 1990s emphasize the extent of institutional stability, the occurrence of limited and incremental changes and the country's resiliency in the face of globalization challenges (Hall 2007; Deeg 2005; Thelen 1991; Harding 1999; Wood 2001; Hassel 2007). Building on the

VoC approach, some scholars have argued that this institutional stability is, in part, the result of employer interests. In this view, their economic interests motivate employers in CME's to defend existing institutions against attempts at liberalizing reforms by other actors.

Kathleen Thelen, for instance, has argued that the relative stability of the German model of industrial relations, compared to its equivalents in liberal market economies, rests in part on the vested interests of large manufacturing firms, which are "unwilling to abandon the German model" (Thelen 2001: 84). Employers' interests in a cooperative workforce and "shop-floor peace" require them to support institutions for labor participation. Specifically, Thelen argues that in CME's

national-level bargaining institutions have been shored up not just by strong unions, but by employers who realize the extent to which the plant-level co-operation that they seek with labor is underwritten and sustained by the collective management of labor markets above the plant level (Thelen 2001: 73).

In a similar way, Peter Hall argues that the "stance taken by producer groups...explains some of the resilience of VoC....Firms were reluctant to endorse institutional reforms that threatened the viability of corporate strategies in which they had made major investments" (Hall 2007: 63). Hall points out that the production strategies of large German firms rest on a cooperative workforce and that, therefore, these firms will defend institutions fostering cooperation with labor against political challenges. Stewart Wood also emphasizes that the interests of German employers are a source of political continuity, rather than change. Analyzing labor market reforms in Germany, Sweden and the UK, he argues that German employers adjusted their production strategies to the existing institutional framework and, once having done so, became defenders of this institutional framework (Wood 2001: 376-9; s.a. Hassel 2007: 254 for a comparable argument). He argues that "German employers since the early 1980s have repeatedly failed to bite when offered the carrot of deregulation by the CDU-led government" (Wood 2001: 408).

These accounts are theoretically informed, in part, by the VoC approach by Hall and Soskice. The VoC approach expects that CME-type institutional frameworks will be backed by cross-class alliances consisting of dominant segments of capital and labor (Hancké et al. 2007: 20). Reform projects will be shaped not so much by class conflicts, but by conflicts between segments of the economy, in particular between large and small firms. Intensified competition brought by economic internationalization and the adjustment of firms to institutional constraints will produce sectoral cross-class coalitions in defense of the existing institutional framework. Hall and Soskice aptly articulate this argument:

In coordinated market economies...governments should be less sympathetic to deregulation because it threatens the nation's comparative institutional advantages. Although there will be some calls for deregulation even in such settings, *the business community is likely to provide less support for it*, because many firms draw competitive advantages from systems of relational contracting that depend on the presence of supportive regulatory regimes. In these economies, *firms and workers have common interests to defend* because they have invested in many co-specific assets, such as industry-specific skills. Thus, the political dynamic inspired by globalization in these countries is likely to entail *less class conflict* and to center around *the formation of cross-class coalitions*, as firms and workers with intense interests in particular regulatory regimes align against those with interests in others (Hall and Soskice 2001: 58, emphasis added by TP).

This analysis in this chapter takes issue with the VoC argument. If we follow the VoC perspective, we should expect that dominant employer groups will oppose deregulatory reforms, and that this is one reason for the failure of such reform initiatives. As Wood correctly notes: “If the Soskicean account of employer preferences is correct, the inability of parties to sustain a radical legislative attack on labor market structures is as likely to be the result of employer pressure as pressure from trade unions” (Wood 2001: 393).

Empirically, however, there is little evidence of deregulatory reforms that would have been opposed by employers, or dominant segments among them, as the following sections try to show. To the contrary, employers have often pushed for deregulatory reforms. Though German employers do not demand the outright dismantling of institutions of social compromise and welfare state programmes, they have become much more assertive in pushing for liberalizing reforms, compared to the post-war period. Rather than defending existing policies and institutions against liberalizing reforms, they promote reforms that move Germany towards a less regulated and less costly type of market economy.

Theoretically, the VoC perspective faces difficulties in capturing the changes in employer positions and strategies that have happened during the 1990s. While the VoC perspective does provide a plausible explanation for why German employers do not push for the outright dismantling of industrial relations and welfare state institutions, it has difficulties explaining employers’ turn away from social compromise at the political level, their campaigning for deregulation and welfare state retrenchment, as well as the erosion of bargaining institutions due to the exit by individual firms. The interpretation by the VoC perspective is at odds with the empirical observation that German employers have often been protagonists, rather than opponents, of liberalizing reforms in labor market and social policies, even if these reform attempts may often have been modest. Its emphasis on employer

interests as a force of stability, rather than change, provides the VoC approach with difficulties in explaining the broader changes in employer positions and strategies.¹³⁹

The remaining parts of this chapter try to show empirically that since the 1990s German employers have become a driving force for institutional reforms in industrial relations and social policies, rather than defenders of *the status quo*. The next section briefly discusses the effects of unification and economic transformation in the East on the politics of German employer associations, before turning to employers' offensives for change in welfare state institutions (III) and industrial relations (IV).

9.II German Unification and the Pacification of the East

German unification resulted in a brief return to social compromise. It temporarily muted existing conflicts over the reform of the German political economy. The West German government responded to unification with the rapid transfer of West German political and economic institutions to the new, Eastern part of the country. Its declared goal was the rapid convergence of East German standards of living and economic conditions to the standards prevailing in the West in order to prevent social unrest. Chancellor Kohl promised East German citizens "flourishing landscapes," a metaphor for economic prosperity. This policy of rapid economic convergence appears to have been motivated by normative and political considerations, rather than by any strict economic rationale (Hefeker and Wunner 2003). The ultimate goal was to ensure the political loyalty of East German citizens to their new state.¹⁴⁰ This policy was initially endorsed by all major political actors, including the employer associations. The political goal was to prevent the consolidation of a socio-economic east-west cleavage, with the potential development of political instability and radicalism in the East if the high hopes of East Germans would be frustrated.

West Germany proceeded quickly with the full-scale extension of its political and economic institutions to its new *Länder*. This included also the extension of the West German framework of economic regulations, its institutions of industrial relations and welfare state programmes. A monetary union with a conversion rate of 1:1 extended the West German *Mark* to the East (Ritter 2007: 145). The West German national government had been the dominant actor in the process organizing unification, whereby labor unions and employer organizations had not been directly involved in the bipartite negotiations leading to the

¹³⁹ For a similar argument see Menz 2005 .

¹⁴⁰ This politically motivated use of social policies shows resemblance to the politics and policies of transformation in other East European countries. An in-depth study by Pieter Vanhuyse shows that governments in these countries used social policies for strategic reasons, to ensure the acquiescence of the population to economic transformation (Vanhuyse 2006).

unification of the two states. Nevertheless, both sides of industry initially supported the policy of institutional extension and rapid economic convergence (Ritter 2007: 223-230). The initial period of unification, up to the autumn of 1992, was characterized by political consensus and close cooperation among all actors, including also employers.

The national employer federation, BDA, agreed that West German institutions and policies should be transferred rapidly to the East, and that transition periods should be kept as short as possible. This applied also to the field of industrial relations. The formal institutional framework of the dual system of industrial relations was extended to East German firms without modification. The transfer of the West German model to the East initially seemed to proceed quickly: labor unions and employer organizations were quickly founded in the East and started to conclude sectoral collective agreements. This was a top-down process orchestrated by the West German unions and employer associations, who controlled their affiliates in the East. As there had been basically no private capital in the GDR, Eastern German employer associations had to be established from scratch, relying on West German initiative. The decision by the state's privatization agency (*Treuhandanstalt*) to oblige the firms it held in trust to join an employer association greatly facilitated their formation in the East (Ritter 2007: 246).

In the initial phase, labor unions and employer associations both agreed on the goal of rapid wage convergence between East and West. In March 1990, DGB and BDA issued a joint declaration supporting a currency union and the extension of the West German industrial relations model to the East, including the stepwise convergence of wages and social benefits, in line with productivity growth in the East (Ritter 2007: 225). In June 1990, employers and unions in the metalworking sector of the East German region of Berlin-Brandenburg reached an agreement on stepwise wage convergence (*Stufenplan*). This plan intended to equalize East German wage rates with West German standards by way of stepwise increases until full parity would finally be reached in April 1994 (French 2000: 203-8). This model was then extended to the remaining East German regions. As a result, hourly wage rates in East German metalworking increased by 68 per cent between 1991 and 1993 (French 2000: 206).

The BDA officially endorsed the unmodified transfer of the West German economic and social model to the East. Some voices in industry had proposed the establishment of a low wage or low tax production zone in the East ("*Sondersteuergelände DDR*"), in particular voices from the BDI and the market liberal FDP party, but the BDA's official position did not reflect these views (Schroeder 2000: 185). These dissenters intended to use unification as a tool for

putting deregulatory pressure on the West German model by creating regulatory competition within the country. The official endorsement of a uniform regulatory environment by the BDA raises the question why the employer federation did not use unification as a window of opportunity to establish a low-wage/low-regulation production zone in the East, as some industry representatives had proposed? *Prima facie*, this appears to confirm the view that dominant groups of German employers genuinely prefer the German high-wage/high-regulation system.

Employers' support for rapid wage convergence and a uniform regulatory environment was motivated by the political and economic considerations of West German employers. As no independent entrepreneurial class existed in the East in 1990, the West German employer associations could exercise great leverage in setting up the wage bargaining system there. Politically, their goal was the pacification of East German workers in order to ensure a smooth and successful integration of Eastern Germany into a capitalist economy and society. Employers acknowledged the need to accompany Eastern Germany's transition to a capitalist economy with social benefits and wage convergence to ensure the pacification of Eastern German citizens. In addition, employers also agreed with the widespread beliefs that productivity in the Eastern German economy would be likely to catch up quickly to Western standards and that the financial transfers needed would therefore only be of a temporary nature (Schroeder 2000: 187).

Economically, West German employers had an interest in preventing the emergence of domestic low-cost competition by firms which would not be subject to the same regulatory constraints than their competitors in the Western part of the country (French 2000: 204-5; Manow and Seils 2000: 286). This calculation clearly reflected the interests of West German employers, rather than those in the East. West German employer associations assumed that productivity in the Eastern economy would catch up rapidly, thus allowing firms in the East to be able soon to pay wages comparable to the West. This calculation, however, neglected the specific technological and economic conditions of East German plants, which prevented a rapid increase in labor productivity. The policy of wage convergence thus led to a rapid increase of unit labor costs in the East, as shown below. In short, the fear of low-cost competition from the East kept the upper hand over the opportunity to exert deregulatory pressure on the West German system.

The policy of rapid wage convergence, together with the one-to-one currency conversion, contributed massively to the collapse of the East German industry. Growth of labor productivity in the East fell short of the high initial expectations and did not keep up

with the rate of wage growth. As a consequence, relative unit labor costs in East German industry stood at 191 per cent of the West German level in 1991 (Manow and Seils 2000: Table 6.1). Massive deindustrialization and labor shedding in East German plants occurred as a consequence. Between 1991 and 1993 total employment in the East fell by 15 per cent, manufacturing employment even fell by 45 per cent (Manow and Seils 2000: 286-7).

The initial period of political consensus after unification came to an end in the autumn of 1992, when the economic problems in the East and the high costs of unification became clearly apparent to all actors (Ritter 2007: 8). Many East German firms responded to the wage policy of their associations by non-compliance to collective agreements, often with the tacit consent of local works councils, or by leaving employer associations in order to avoid collective bargaining altogether, as is shown in more detail below (section IV). According to a survey of 700 East German firms conducted in 1996, 43 per cent of covered firms did not fully comply with sectoral agreements (Ritter 2007: 249).

When these problems became apparent, the employer associations decided to change course. In March 1993, the metalworking employer association declared an “extraordinary termination” of the wage convergence agreement with *IG Metall* and demanded its renegotiation. Metalworking employers proposed a 9 per cent increase for 1993, instead of the 26 per cent originally agreed in the *Stufenplan*, plus an exemption clause for firms in serious economic difficulties (French 2000: 206-7). Unions reacted with “warning strikes” and declared the termination of the agreement illegal. In May 1993, a pilot compromise was reached in the district of Saxony, which was later extended to the rest of Eastern Germany. The compromise postponed full wage convergence for two years, until 1996, and introduced a special “hardship clause” for firms with serious problems.

According to this hardship clause, management and works councils of a firm could apply to the collective bargaining partners to be exempted from the terms of the collective agreement, if the firm faced serious economic problems. If accepted by the bargaining partners, the exemption allowed the firm to undercut the conditions of the collective agreement (Hassel 1999b: 497). To apply, firms needed to open their books and present a strategy for recovery. The renegotiation of the *Stufenplan* allowed thus a greater differentiation of wages and working conditions, although within the limits accepted by the collective bargaining partners. BDA president Klaus Murmann later admitted that the policy of rapid wage convergence had been a mistake. In response to the question “How big is the

responsibility of a mistaken wage policy for unemployment in Eastern Germany?” he answered:

The employer associations bear great responsibility, and, if you like, complicity. Just as I admit that I belonged to those, who, during the turnaround of 1989/1990, expected that productivity and incomes in the East would converge quickly; so I also belonged to those who in 1992/93 tried tooth and nail to revise and dismantle these *Stufenverträge* of rapid wage convergence (Murmann 1997: 110).

To sum up, German unification in 1991 had triggered a brief period of class consensus and compromise, which was shaped by the joint commitment to extend the West German economic model to the East. This short period came to a sudden end in late 1992, when employers realized the high costs of economic transformation in the East. The policies of unification and economic convergence exacerbated the economic woes of the East, by making East German firms uncompetitive, and thereby contributed to the erosion of collective bargaining institutions in the East in the subsequent years (see section IV). The social costs of deindustrialization in the East were shouldered by the West German welfare state, thereby contributing to the continued rise in non-wage labor costs, one of the main reasons for employers rising dissatisfaction with existing policies and their turn away from social compromise.

9.III Employers' Offensive for Welfare Retrenchment

The social consequences of deindustrialization in the East were cushioned by the West German welfare state. The political consensus during the early period of unification (1990/1991) included also the use of social benefits for cushioning economic transformation in the East. West German welfare state programmes were extended to the East and benefit levels there were raised to West German standards. Active labor market policy measures, in particular job-creation schemes, were expanded on a massive scale in the East during the early years after unification, but such measures were often perceived as ineffective and as intended merely to keep unemployed persons out of mischief. They were later cut back to reduce costs (Ritter 2007: 488). In addition, unemployment insurance and early retirement were used on a massive scale to cushion the effects of economic restructuring (Manow and Seils 2000: 292-5). In 1992, social expenditures in the East amounted to 66 per cent of its GDP (Ritter 2007: 485). In short, large-scale financial transfers from the West to the East cushioned the social consequences of economic transformation.

The costs of this policy of economic restructuring-cum-social pacification were financed by various revenue-raising measures: higher payroll taxes, additional state subsidies

to the social insurance funds, as well as several ad-hoc measures to raise tax revenues, such as a temporary “solidarity surcharge” on income tax. Together with high levels of unemployment and early retirement also in West Germany, the extension of the West German welfare state to the East had thus contributed to the long-term rise in non-wage labor costs in Germany (see table 9.2 below). Total payroll taxes increased from 35.5 per cent in 1990 to 42 per cent in 2003, thereby continuing the sustained rise of payroll tax rates that occurred already during the previous decades.

Table 9.2 Total payroll taxes in Germany (1949-2003)

Year	1949	1953	1958	1963	1968	1973	1978	1983	1988	1993	1998	2003
%	20.0	20.0	24.4	25.0	26.5	28.9	32.4	34.9	35.9	37.2	42.1	42.0

Source: Streeck and Trampusch 2005: Table 1 Note: payroll tax rates are as a percentage of gross wages and are paid in part by the employer, in part by the employee.

Employers’ push for cost-cutting reforms

Under pressure from international cost competition, employers became increasingly reluctant to put up with the sustained rise in labor costs. Reducing non-wage labor costs became the paramount political concern of German employers during the 1990s. They demanded a reorientation in social policy, including substantial cutbacks in social benefits, lower payroll taxes and more self-reliance by the individual. The federations representing smaller firms, like the *Federation of German Artisans* (ZDH), used to take a particularly aggressive stance. The ZDH demanded, for instance, a substantial reduction in social expenditures (e.g. *Sueddeutsche Zeitung*, 22/06/2005: 23; *Sueddeutsche Zeitung*, 25/04/2002: 24), an extension of the low-wage sector (*Sueddeutsche Zeitung* 24/12/2001: 5) and the abolition of dismissal protection (*Sueddeutsche Zeitung*, 25/04/2004: 24).

Lobbying for welfare state retrenchment was, however, by no means limited to small firm associations, but also became a priority for the national employer federation, the BDA, which is dominated by larger firms. Due to the internal division of labor among German business federations, the BDA is the federation that is in charge of social policy and labor market issues (Grote et al. 2007: 160-2). In addition to issuing opinions on specific pieces of legislation, the BDA also articulates more general and programmatic positions in media statements and through various publications and public relations campaigns. In the 1990s, the BDA has shifted from a responsive strategy, reacting to policy initiatives by other actors, to a

more proactive strategy, actively demanding reforms. This shift is visible, *inter alia*, in the fact that from 1994 on the BDA has regularly issued policy manifestos demanding comprehensive social policy reforms¹⁴¹ (BDA 1994, 1998, 2002, 2005).

Rather than directly dismantling Bismarckian welfare state institutions, the policies proposed by the BDA aim at transforming the Bismarckian welfare state from within. The manifesto of 1994, entitled “*Reconstructing Social Security*” (BDA 1994) envisaged the possibility of considerable cost reductions within the existing institutional framework of the Bismarckian welfare state, by abolishing those benefits and services considered as not essential and by encouraging more self-reliance, instead. In particular, the BDA demanded that financing of active labor market policies be shifted from payroll taxes to the general state budget (s.a. Murmann 1997: 159). Social insurance programmes should remain financed by payroll taxes but should be freed from financing so-called “non-insurance benefits,” which includes measures such as active labor market policies and various non-actuarial benefits.

Four years latter, in 1998, the BDA published another policy manifesto, entitled “*Social Policy for more Competitiveness and Employment*” (BDA 1998). The BDA demanded that the ambitions of the welfare state should be reduced from providing income maintenance benefits (“*Lebenstandardsicherung*”) to providing only a minimum standard of protection (“*Basissicherung*”), in order to reduce non-wage labor costs (14). Moreover, the BDA demanded deregulation in labor law and of wage policies (10-11). Wage bargaining functions should be decentralized, with more scope being given to bargaining at the plant level, with greater differentiation of wages to allow the growth of a low wage sector, and with sectoral agreements being transformed into a regulatory framework defining only minimum standards, rather than actual conditions (10-11). Another manifesto, published in 2002, “*A New Departure in Social Security*” (BDA 2002), repeated the known demands for a downsizing of the welfare state by re-focusing social policies on their “core competencies” and combining public and private provisions (4-5).

Subsequent manifestos, entitled “*Promoting Growth and Employment*” (BDA 2005) and “*Principles for a Reorientation of Social Insurance*” (BDA 2006), again emphasized

¹⁴¹ These policy manifestos are approved by the BDA’s Board of Directors and can thus be considered to represent lowest common denominator positions. Another indicator for the new pro-active stance is the changing nature of the annual reports published by the BDA. Up to the early 1990s, these reports were often more than 100 pages long and dealt in detail with the BDA’s positions on specific pieces of legislation. Since then, the reports have become much shorter and focus, instead, on general programmatic statements, emphasising the need for radical welfare state reforms. This shows the new emphasis of the federation on shaping public opinion on the general direction of reforms, rather than on shaping the details of policies through cooperation with government policy-makers.

demands for cost-cutting reforms in the welfare state to maintain international competitiveness. This time, a shift in the financing of health care and long-term care insurance away from payroll taxes is also advocated, unlike in the previous manifestos (BDA 2002). Financing of these two programmes should be transferred to individual insurance premiums unrelated to earnings. Health care and long-term care insurance should only provide primary services, patient co-payments should be extended and market mechanisms of governance should be strengthened (BDA 2005: 7). The principle of mandatory coverage in social insurance should be maintained in order to avoid adverse selection problems (BDA 2006: 3-4). Redistributive elements within the social insurance system should be systematically eliminated (BDA 2006: 4-5). In pensions and unemployment insurance, payroll tax financing should be maintained, and benefits be kept strictly earnings-related (i.e. actuarial), in order to maintain work incentives (BDA 2005: 9, 13; 2006: 5). The duration of unemployment insurance benefits should be shortened further and the statutory retirement age should be raised to 67 (BDA 2005: 9). Dismissal protection should be made more flexible (15).¹⁴²

The BDA's reform proposals amount to a substantial downsizing of the German welfare state. The BDA does not advocate a radical transformation to the model of a liberal-residual welfare state, though. The proposals maintain the basic institutional framework of the Bismarckian welfare state. Payroll tax financing, earnings-related insurance benefits and mandatory insurance coverage, the defining institutional features of Germany's conservative welfare state model shall, by and large, be maintained.¹⁴³ However, the reform proposals of the BDA do in sum amount to a substantially less generous and less redistributive welfare state, a further decentralization and deregulation in industrial relations and greater income

¹⁴² Positive effects of social policies on economic competitiveness are mentioned nowhere in the BDA documents. In contrast to what the skill formation thesis by Estevez-Abe et al (2001) predicts, the BDA expects that high non-wage labor costs, caused by high levels of social spending, have a *negative* effect on skill investments and work incentives because high non-wage labor costs reduce the relative net salary of employees. (BDA 2006: 5-6) (2001).

¹⁴³ The BDA's preference for Bismarckian welfare state programmes results from its role in social insurance administration, which provides it with a vested organizational interest in this type of welfare state organization. Like the labor unions, employer associations participate in the administration of social insurance programmes and labor market policies ("social self-government") and thereby have a certain, albeit very limited, influence over expenditures and payroll tax levels. Employer associations and labor unions are both determined to defend their organizational role in social policy administration and prevent direct state interventions in this domain (e.g. Murmann 1997: 163-4). A shift away from payroll tax financing also undermines the legitimacy of their administrative involvement, as without a contribution to financing also the legitimacy of their involvement in administration would appear questionable. Moreover, employers' reluctance to push for a shift away from payroll taxes appears to be motivated also by a scepticism about whether such a switch would actually result in a lowering of the total cost burden on firms. A rise in income tax, for instance, would potentially also be born by firms via compensatory wage demands and, possible, also an increase in industrial conflicts.

inequality. The BDA reform programme combines continuity in the formal institutional framework with substantial changes in socio-economic outcomes.¹⁴⁴

The BDA positions presented above illustrate the more assertive and less accommodating stance by German employers. Unlike in the past, the federation is now actively trying to set the agenda for reforms, rather than merely responding to reform initiatives by other actors. While during the period of welfare state expansion employers had been in a passive and reactive position, trying to contain reform efforts made by other actors, they now became a driving force for reforms. The change in welfare state politics from expansion to containment made it more expedient for employers to take a more assertive stance and also to move away from consensual policy-making.

Care insurance: a political Waterloo for employers

While the general focus of welfare state politics in the 1990s was on cost containment, some expansionary reforms still occurred. The most important expansionary reform during the 1990s was the introduction of a pay-as-you-go financed programme for long-term care insurance in 1994. Employers were fighting unsuccessfully to prevent it. The reform was initiated by the Christian Democratic Minister of Labor, Norbert Blüm, a proponent of the party's labor wing. The issue divided the Christian Democrats. Its labor wing and the churches favored public long-term care insurance. Social democrats and labor unions also favored it. The free market wing within the CDU, spearheaded by the party's business groups, opposed care insurance. The issue was finally decided when Chancellor Kohl, who had initially been skeptical of care insurance, changed sides. Motivated by the electoral potential of the elderly, the government finally decided in June 1993 to go ahead with care insurance (Ritter 2007: 265).

The BDA and other business federations lobbied vehemently against a public and pay-as-you-go financed care insurance, because of the anticipated rise in labor costs, but did not succeed.¹⁴⁵ They presented an alternative model for care insurance, but only relatively late in the reform process (Murmann 1997: 165-6) (*Sueddeutsche Zeitung*, 15/09/1993). This so-

144 Georg Menz has coined the phrase "old bottles with new wine" to describe this phenomenon (2005: 196).

¹⁴⁵ After the introduction of care insurance, the BDA shifted its demands towards cost-cutting measures in care insurance: benefits should become limited to severe types of care needs and provide only a basic level of protection, and private, pre-funded arrangements should be promoted by the state (BDA 2002: 11-13). Since 2005, the BDA also demands a shift in the financing of care insurance from payroll taxes to individual premiums (BDA 2005: 7).

called “dual component model”¹⁴⁶ consisted of mandatory private care insurance, based on pre-funding, for all Germans above the age of 25. In addition, a public transition fund should be established for those already too old to accumulate savings (Ritter 2007: 693-5). BDA president Murmann had later called his failure to prevent public care insurance “the greatest fiasco of my term in office” (Murmann 1997: 165).

The example of long-term care insurance shows that when expansionary reforms appeared unstoppable, as in this case, employers still resorted to their old strategy of political accommodation, by presenting alternatives intended as compromise proposals. The case of long-term care insurance has, however, also shown to employers the ineffectiveness of their strategy of political accommodation. The failure of employers to prevent long-term care insurance is likely to have contributed to their subsequent turn away from political accommodation and towards a less conciliatory and more assertive strategy. Employers realized that, instead of only reacting to proposals brought on the agenda by other actors, they needed to try to proactively define the reform agenda.

Alliance for Jobs: failure of reform by compromise

Employers’ turn to political confrontation is also reflected in the failure of the so-called *Alliances for Jobs* talks to produce meaningful reform compromises. Two consecutive governments initiated these tripartite talks with a view to forge corporatist compromises on labor market and welfare state reform. The first *Alliance* (1996-98) was set up by the CDU-FDP government led by Helmut Kohl. The talks were later revitalized by the SPD-Green government led by Gerhard Schröder (1998-2001). Both initiatives failed to produce substantial reform packages due to deadlocks between employers and unions and the unwillingness of both governments to override one of the two sides (Bruff 2008: 116-35; Schirm 2002: 229).

Employers and unions both rejected compromise packages, albeit for different reasons. Both sides wanted to exclude certain issues from the talks, leaving little room to forge an encompassing compromise (Hassel 1999a; Merkel et al. 2008: 82-3; Schroeder 2003a: 129; Streeck and Hassel 2003: 114-6). In particular, unions did not want to touch upon wage policy, insisting that this is the prerogative of the sectoral bargaining partners (FAZ, 18/01/2002; FAZ, 15/03/2001). Employers insisted on significant reductions in non-wage labor costs and urged the unions to show wage moderation. They refused to agree to reform

¹⁴⁶ The dual component model was presented by the BDA, and supported by the other business federations, BDI, ZDH and DIHT

compromises and threatened to leave the talks, because they thought that the discussed proposals did not go far enough in meeting their demands for lower labor costs (*Der Spiegel* 01/03/1999: 26).

The failure of both *Alliance* initiatives to produce significant reforms also reflects the institutional weakness of corporatist concertation at the political level. While corporatist cooperation is well institutionalized in industrial relations and social insurance administration, Germany never managed to establish corporatist institutions at the macro-political level, despite several attempts to establish such institutions. The tripartite *Concerted Action* talks from 1967 to 1977, intended to secure wage moderation, managed to produce concrete results only during their early years and remained largely a symbolic institution. Like the Alliance for Jobs, also the Concerted Action failed to develop into a stable institutional form of corporatist concertation.

The *Alliance for Jobs* had to compete with other institutions as a decision-making forum. Important reform issues that might have been suitable for a corporatist reform compromise, such as pensions and tax reform, were decided unilaterally by the national government, without involving the Alliance. In wage policy, the unions insisted on the autonomy of sectoral bargaining and wanted to keep wage policy issues off the Alliance agenda, as mentioned above. For employers, their ability to forge plant-level “employment pacts” with their workforce alleviated the pressure to accept a political compromise on the national level (see section IV). BDA president Dieter Hundt, for example, emphasized that “‘Alliances for Jobs’ belong into the enterprises. Only there can we maintain employment and training places and create new ones” (FAZ, 02/12/1998). In short, the divergence of preferences and the lack of government intervention caused the talks to fail (s.a. Martin and Thelen 2007: 32). The failure of the Alliance talks appears to have strengthened the view among employers that political confrontation is needed to achieve the desired cost-cutting and market-oriented reforms. After the failure of the talks, employers intensified their public campaigning for reforms.

The *INSM*: Taking On Public Opinion

Over the course of the 1990s, public campaigning became employers’ main tool for promoting market-oriented reforms. By way of public campaigning employers tried to hammer the *Standortdebatte* [‘competitiveness debate’] into public opinion, and thereby shape the political agenda in favor of market-oriented reforms. The most prominent and influential of these campaigns is the so-called ‘*Initiative New Social Market Economy*’

(INSM). The INSM was initiated in 1999 by the national employer federation for the metalworking sector, *Gesamtmittel*, which is also the campaign's primary source of funding. The foundation thus occurred at about the time when it became evident that attempts to achieve big reforms through tripartite compromises were stalling. The declared aim of the campaign is to shift public opinion in favor of market-oriented reforms (Speth 2004: 36). The campaign is governed by an advisory board, which is dominated by representatives of *Gesamtmittel* and other business associations (Speth 2004: 39).

INSM combines think tank activities and public campaigning. Despite its dependence on business funding, it presents itself in public as a non-partisan and experts-based organization. With an annual budget of about 10 million Euros, INSM has financed a wide range of campaigning activities. The INSM launched advertising campaigns and newspaper articles, produced teaching material for schools, gave awards to market-oriented politicians, carried out policy studies, and established a network of affiliated academics and politicians, which are paid by the campaign to give public lectures and media interviews or to participate in TV talk shows. Its aggressive campaigning tactics, including for instance covert advertising, have resulted in public criticism of the initiative.

The messages of the campaign focus on the need for market-oriented reforms. The initiative's understanding of the concept of "social market economy" is inspired by the thinking of German *ordo-liberals* of the post-war period (e.g. Müller-Armack 1948; Röpke 1950), including the former CDU Minister of Economics *Ludwig Erhard*, whom the INSM presents as a model of sound economic policy-making. As elaborated in chapter 6, the core doctrine of the "social market economy" school is the argument that free market competition is the best tool for achieving social justice. State regulation should serve to promote free market competition, not to constrain it (Friedrich 1955: 511; Haselbach 1991: 172; Mudge 2008: 715). This doctrine was popularized in the 1950s by Erhard, who acted as the public relations spokesperson of this school (Friedrich 1955: 510). Although the social market economy has since remained a vaguely defined concept, meaning very different things to different people, it has become akin to a foundational myth for Germany's post-war political-economic order and is frequently evoked in political discourse (e.g. *Die Zeit*, 03/05/2007: 27). The INSM tries to link its campaign to the positive normative connotations that this concept enjoys in public discourse.

In contrast to the way these concepts are commonly understood today, the INSM tends to use the two concepts 'neo-liberalism' and 'social market economy' in a synonymous way.

On its website (www.insm.de), the initiative states that “neo-liberalism is...a differentiated social science theory and the most important source of Ludwig Erhard’s policy of the Social Market Economy” (INSM 2007). The initiative defines neo-liberalism as follows:

The central value of neo-liberalism is freedom. What is meant by that is not the untamed freedom of anarchy, but the ordered freedom of a state, where the common law stands above the interests of the individual. The fundamental insight of neo-liberalism is thus: freedom requires order (INSM 2007 ,translated by TP).

Gesamtmetall’s sponsoring of INSM shows that employers have identified public opinion as an obstacle to the kind of reforms they want. The decision to found and fund INSM was made after opinion polls had shown that large parts of the German population supported a generous welfare state and opposed market-oriented reforms (Speth 2004: 7). *Gesamtmetall* mandated the initiative to conduct public relations campaigns with a view to produce a long-term change in public opinion in favor of market-oriented reforms. *Gesamtmetall* instructed INSM to focus on general programmatic statements, and not to develop specific policy proposals or to intervene in specific policy conflicts¹⁴⁷ (Speth 2004: 36-7). The campaign shows that employer associations are expanding their strategic focus from a short-term strategy of influencing specific legislative projects to a long-term strategy of pro-actively trying to define the political agenda and shaping public opinion.

Hartz reforms: abandoning social compromise

After the failure of the Alliance for Jobs, the Schröder government *de facto* abandoned attempts to forge a corporatist compromise and decided to go ahead with reform measures unilaterally, instead. In February 2002, shortly before the national elections, the government decided to set up an expert commission mandated with making proposals for job-creating labor market reforms. The commission consisted of 15 members, including, *inter alia*, representatives of the social partners, individual enterprises and business consultancies. The commission was named after its chair, the personnel director at VW, Peter Hartz. With this

¹⁴⁷ The INSM avoids directly attacking other political actors and their positions. This holds also with respect to the unions. As the employer associations negotiate collective agreements with the unions, they continue to have a strong interest in maintaining cooperative relations with the latter and thus avoid any anti-union rhetoric. As shown below, the employer associations have responded to increasing dissatisfaction with the existing collective bargaining system among their members by trying to negotiate reforms with the unions. Public agitation would be counter-productive for achieving a negotiated compromise. This aspect is evident in the fact that INSM is not allowed to address issues of wage bargaining (Speth 2004: 7-8, 41-2). Their commitment to negotiated compromises in the field of collective bargaining provides the employer associations with an interest in keeping wage policy out of public controversy. The neo-liberal approach is thus not followed through consequently in the field of wage bargaining, the employer associations’ genuine policy domain, and aims instead primarily at a reduced role of the state. Generally speaking, though, the turn to public campaigning indicates a turn away from political compromise and corporatist bargaining, and towards a more confrontational and politically radicalised stance.

initiative the government intended to set a signal that it is determined to act against unemployment, whereby the setting up of the commission was facilitated by a report about mismanagement within the public job placement services, underlining the need for reform (Kemmerling and Bruttel 2006: 9). The initiative was also intended to sideline unions as veto players by shifting decision-making to an apparently non-partisan expert group, where the unions would be in a minority within the committee. The commission's proposals were in general in line with business preferences and were, in principle, endorsed by the business federations. They aimed at supply-side reforms of the labor market, in particular measures to improve labor market flexibility, to encourage the personal initiative of the unemployed ("activation"), to tighten work obligations, as well as organizational reforms of the job placement services.

The report by the *Hartz Commission* inspired a bundle of government reform measures, which were translated into four laws passed by parliament in December 2002. The reform measures, included, for instance, start-up grants for self-employment (*Ich-AG*), the promotion of temporary work agencies and a reorganization of the public job placement services. The most controversial component of the reform package was a comprehensive reform of the system of passive labor market policy, intended to strengthen the work incentives of the unemployed (*Hartz IV* reform). This reform strengthened the work requirements of the unemployed, shortened the benefit duration in unemployment insurance, and strengthened means-tested elements in labor market policy by introducing a new programme of unemployment assistance (ALG II) for the long-term unemployed (Merkel et al. 2008: 84-7).

After its re-election in 2002, the Schröder government extended its new course of unilateral welfare state reform, without consulting first with the social partners, through the so-called *Agenda 2010* program. This program consisted of a bundle of labor market and social policy reform measures, intended to reduce payroll taxes to a level below 40 per cent by cutting benefits, explicitly justified by the need to maintain Germany's international competitiveness (Bundesregierung 2003; Hüther and Scharnagel 2005: 28). The Hartz reforms and the Agenda 2010, both fully supported by the business federations, reflect the new political agenda of improving competitiveness, which employers promoted throughout the 1990s with their *Standortdebatte*. The passing of these reforms appears to be due, in part, also to the success of employers to shape the political agenda by impressing the need for cost-cutting reforms upon the public and thereby ensuring the public acceptance of these reforms.

9.IV Industrial Relations: Employers' Offensive for Decentralization

Developments in industrial relations parallel those in welfare state reform: An increasing dissatisfaction with existing institutional arrangements turned employers into protagonists of institutional change. Considerable tensions in the German model of industrial relations have emerged, with employers demanding more decentralization and flexibilisation in collective bargaining. Individual firms have tended to abandon sectoral bargaining, and, hence, employer associations tried to renegotiate collective bargaining institutions with unions. Employers have either chosen “voice”, pushing for decentralization and flexibilisation within the existing institutional framework, or “exit”, dropping out of sectoral bargaining completely.¹⁴⁸ As a result, the coverage of the German model of industrial relations has been shrinking and its character been transformed by changes going on within it. These changes have been driven primarily by the employer side and its dissatisfaction with the outcomes produced by the existing bargaining system.

A considerable share of German firms has lost confidence in the German model of industrial relations and has left sectoral bargaining, thereby causing the coverage of the model to shrink and creating pressures for its reformation. Sectoral bargaining is a voluntary institution in Germany, whereby the agreements are legally binding only for those firms and employees that are organized in one of the signatory parties.¹⁴⁹ Because in Germany the organizational strength of employers is much higher than that of unions, the ability of employer associations to retain their members defines to a large extent the bargaining coverage rate. The declining coverage rate is due to firms leaving their associations, rather than to declining union strength.

Table 9.3 Organizational Strength of *Gesamtmittel* (employee density rate)

Year	Gesamtmittel Employee Density Rate – West Germany	Gesamtmittel Employee Density Rate – East Germany
1970	73.3	NA
1980	72.7	NA
1985	73.8	NA
1989	70.3	NA
1991	71.6	65.7

¹⁴⁸ The concepts of “exit”, “voice” and “loyalty” were first developed in Hirschman 1978

¹⁴⁹ An exception to this is where the state makes use of its powers to extend coverage of an agreement to all employees in the sector. Usually, firms offer collectively bargained conditions also to non-unionised workers.

1993	63.3	60.0
1998	64.8	32.2
2003	59.0	21.0
2004	57.6	18.1

Source: Hassel (1999b: Table 7) and Streeck (2003: Table 3) .Data for 2003 from Schnabel (2005: 186) data for 2004 from Silvia and Schroeder (2007: 1440-1). NA: not applicable.

Dissatisfaction with sectoral bargaining is the main reason why firms leave their association. In a survey among firms that had left their association, 75 per cent of the responding firms cited dissatisfaction with collective agreements as their main reason to resign¹⁵⁰ (Schroeder and Ruppert 1996: 327). The organizational strength of employer associations is thus a good indicator of the extent of employer support for sectoral bargaining institutions. Precise membership data are only published by *Gesamtmittel*, the peak employer association for metalworking. With metalworking being the core of German manufacturing industry, *Gesamtmittel* is also the largest sectoral employer association and plays a leading role in the collective bargaining system, where the metalworking sector acts as a pattern-setter¹⁵¹.

The development of its *employee density rate*, the percentage of sectoral employees working in an organized firm, shows a substantial decline in organizational strength since the mid-1980s. At that time, employee density peaked at 74 per cent. Since then, employee density declined to 58 per cent in the West and 18 per cent the East (see table 9.3 below). Organizational density in West German metalworking has thus declined by 16 per cent within two decades. Organizational strength is much lower in Eastern Germany, where many firms left their associations after the first few years following unification, or, in the case of newly established firms, decided not to join an employer association from the outset.

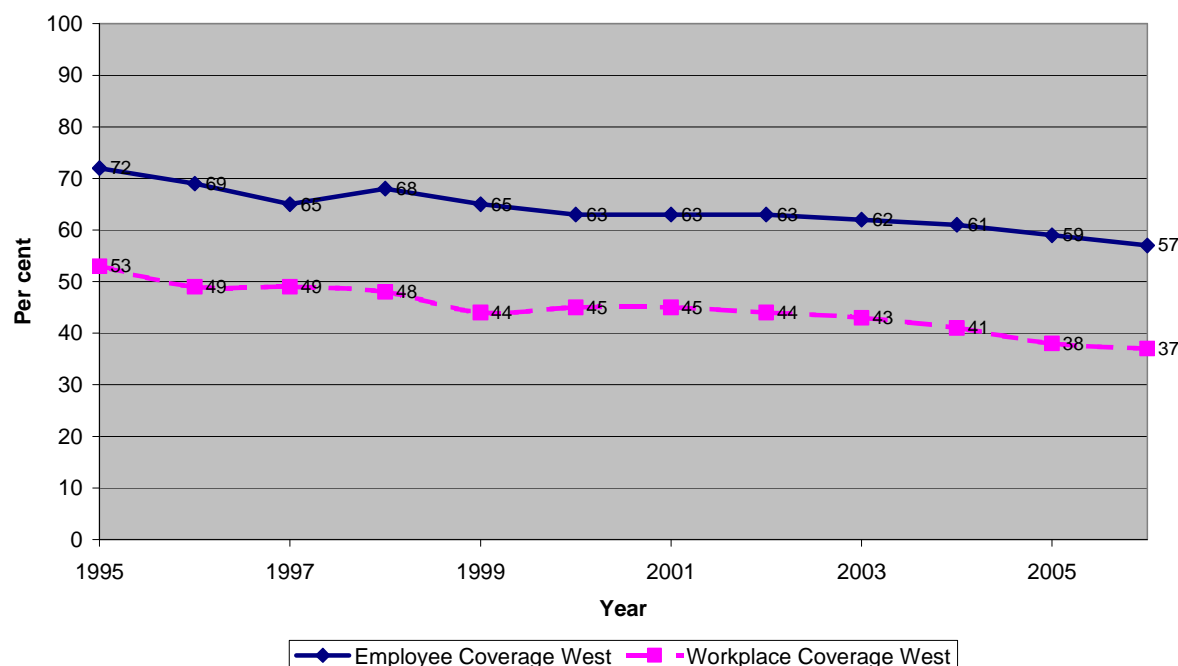
The decline in employers' willingness to participate in sectoral bargaining is evident in the development of bargaining coverage rates. According to a yearly survey among 16,000 firms done by the IAB – the research institute of the National Employment Agency -

¹⁵⁰ 34 per cent mentioned dissatisfaction with association services and 37 per cent mentioned high membership fees. Multiple answers were possible.

¹⁵¹ It is estimated that *Gesamtmittel* alone contributes about 50 per cent to the budget of the national employer federation BDA (Grote et al. 2007: 168-70). Due to its financial strength it therefore also has a great say in the peak federation's policymaking.

coverage by sectoral agreements has declined by about 15 per cent in West Germany between 1995 and 2006 (see chart 9.2 below). About 40 percent of all employees in the West, and about 60 per cent in the East, are not covered by sectoral collective agreements anymore.¹⁵² This decline in bargaining coverage is the result of changes in employer strategies, increasingly unwilling to put up with the constraints of social compromise. The declining coverage rate shows that an increasing share of German firms is not backing the ‘German model’ anymore.

Chart 9.2 Coverage rates by sector-level bargaining (1995-2006)



Note:

Employee coverage: percentage of all employees covered by sectoral collective agreements

Workplace coverage: percentage of all workplaces covered by sectoral agreements

Source: Schnabel 2005: 190 (Fig.3) and Ellguth and Kohaut 2008: 515 based on data from the IAB establishment survey (*IAB Betriebspanel*).

The likelihood of firms abandoning sectoral bargaining is structured by firm size and union strength. Studies by Schnabel and Wagner and by Ruppert and Schroeder have shown that the likelihood of firms resigning from their association is disproportionately high among smaller firms, firms with a low level of workforce unionization and firms with low strike risks (Schnabel and Wagner 1996; Schnabel 2005; Schroeder and Ruppert 1996: 316-8; Schroeder 2002: 72). Larger firms and firms with a high unionization rate are those most likely to remain organized. One of the main reasons for firms to be a member of an employer

¹⁵² In addition, also the representation of employees by works councils has declined over time. Whereas in 1981, 50 per cent of all employees in the private sector were represented by a works council, this number has declined to 40 per cent in 1994 (Hassel 1999b: 489, Table 2).

association is their interest in industrial peace, protected by the peace obligation of the signatory unions, and the protection against the costs of industrial conflict by the associations' strike insurance funds. Firms need to balance these advantages of sectoral bargaining with the constraints imposed on them by sectoral agreements. The declining bargaining coverage rates indicate that the share of firms that sees the benefits as outweighing the costs is declining.

Table 9.4 Coverage by collective agreements (2003)

Covered by	Sectoral agreement - West	Sectoral agreement - East	Company agreements – West	Company agreements - East	No collective agreement - West	No collective agreement – East
% of firms	42.6	20.9	2.7	5.0	54.7	74.1
% of employees	62.1	42.6	7.6	11.4	30.3	46.0

Source: Schnabel 2005: Table 2

The relationship between firm size and propensity towards collective bargaining has inverted over time. While during the late 19th century, sectors dominated by small firms were the first ones to accept collective bargaining, small firms are today those most likely to resign from collective bargaining. The larger propensity of smaller firms to stay out of sectoral collective bargaining is evident from comparing the rates for employee density with those for firm density (see table 9.4 above). Small firms have become increasingly dissatisfied with the wage policies of their associations, which is shaped by the larger members, as voting rights in employer associations are linked to firm size. The differences between small and large firms in respect to collective bargaining appear to result from differential capacities to deal with intensified cost competition and rising labor costs.¹⁵³

Large manufacturing firms have tended to respond to intensified cost competition by passing on the cost pressures to their supplier firms, as a study by Silvia and Schroeder shows (Silvia and Schroeder 2007: 1445-6). To illustrate their argument these authors cite a practice by *Jose Ignacio Lopez*, a leading purchasing manager in the car industry, who, with each renegotiation of a supplier contract demanded that the supplier cut prices by at least 25 per cent, whereby non-compliant firms would lose the business (Silvia and Schroeder 2007: 1445; s.a. Streeck and Hassel 2003: 110). By shifting pressure to suppliers, large manufacturing

¹⁵³ The rising labor costs are not so much the result of radical wage demands by unions, or employer associations agreeing to overly generous wage agreements, but most of all the result of rising non-wage labor costs (see Table 9.2 above).

firms managed to deal with intensifying cost competition and rising labor costs. Smaller supplier firms, however, had difficulties to keep up with the rising cost pressures and saw abandoning collective bargaining as the only way to reduce labor costs (Thelen and Wijnbergen 2003: 870). Schroeder and Silvia thus conclude that “greatly intensified cost and quality pressures in the wake of globalization [are] the main explanation for the overall decline of membership in German employers associations and the disproportionately large drop in SME density” (Silvia and Schroeder 2007: 1446).

The Associations’ Responses to Bargaining Exit

Employer associations responded to these new challenges in two ways. First, they tried to reform the bargaining system by decentralizing bargaining competencies and making regulations more flexible, in order to ease the constraints on individual firms. Second, they introduced new membership categories that allowed firms to stay out from sectoral bargaining altogether, without resigning from their association completely. Employers were the driving force behind reforms aimed at more decentralized and more flexible bargaining arrangements. So-called “hardship clauses” and “opening clauses” have been included in sectoral agreements, with the intention to provide more scope for plant-level deviations (Hassel 1999b: 496-98). They allow local management and works councils to agree on deviations from sectoral standards. *Hardship clauses* were introduced in East Germany for use by firms in temporary economic difficulties. According to these clauses, firms can apply to the bargaining parties for permissions to deviate, whereby they need to obtain the consent of both bargaining parties to be allowed to deviate from standard conditions (see also section II above).

Opening clauses are not limited for use by firms in financial difficulties but are intended for more general and less conditional use. They often form the basis for plant-level “employment pacts” between management and workforce, whereby deviations from sectoral standards are exchanged against job or investment guarantees (Rehder 2003). The intention of opening clauses is thus to introduce more plant-level flexibility into sectoral collective agreements and to ease regulatory constraints on individual firms. Typical measures introduced by way of opening clauses are greater working time flexibility, lower compensation for overtime work or temporary undercutting of sectoral wage standards to prevent layoffs or a relocation of production (Silvia and Schroeder 2007: 1452). According to Bispinck and Schulten, about one third of all covered firms make use of some forms of bargained deviations from sectoral standards (Bispinck and Schulten 2003).

The decentralization of bargaining through hardship and opening clauses, and the use of plant-level “employment pacts,” indicates a strengthening of the employer side. As economic globalization has made exit threats by firms more credible, management can now more effectively put pressure on labor to make concessions. This pressure can be exercised more effectively on the plant-level than on the sectoral level, because of the greater vulnerability of individual plants to job cuts or relocation of investments.¹⁵⁴ Consequently, the decentralization of bargaining competencies is typically accompanied by “concession bargaining” between plant management and works councils. Promises by management concerning plant-specific investments or job guarantees are linked to concessions by the works council, such as wage cuts or more flexible working time. As a consequence of these plant-level employment pacts wages and working conditions are becoming more diverse across firms, and the capacity of sectoral agreements to set uniform wages and working conditions erodes. Employers do, however, tend to find the decentralizing measures introduced so far as insufficient and promote further flexibility (Silvia and Schroeder 2007: 1452).

Local concession bargaining means that concessions are now made *by* labor, and not *to* labor. Plant-level concession bargaining indicates a declining ability or willingness of individual firms to oblige with sectoral standards. An increasing number of firms appears to be unable or unwilling to cope with the institutional constraints of sectoral bargaining and is seeking plant-level deviations that take into account the specific circumstances of the plant. Even so, the decentralizing clauses that have been introduced appear to have been insufficient to stop bargaining exit. In East Germany many firms have decided to openly violate the terms and conditions of collective agreements in order to avoid massive labor shedding, often with the tacit consent of the works council (Hassel 1999b: 498-90; Thelen 2001: 83). Not all of the decentralization is thus happening within the framework of existing bargaining institutions. It is also happening outside, by firms violating sectoral agreements or resigning from sectoral bargaining entirely. As the epigraph to this chapter shows, this practice was even explicitly approved by BDI president Henkel in a press interview. The intensifying demands from firms for more plant-level flexibility in wage setting and working time arrangements puts the employer associations under pressure to strive for even greater decentralization of collective bargaining, if they want to avoid a further erosion of bargaining coverage.

¹⁵⁴ See Menz 2005 and Raess 2006 for similar arguments

In addition to decentralizing collective bargaining, employer associations have also tried to stop the erosion of organizational strength by developing new categories of membership that do not oblige firms to stick to sectoral agreements. Firms can now normally be a member in an employer association without having to accept collective bargaining. These “opted out-members,” or so-called “*OT members*” (“*ohne Tarifbindung*”), enjoy access to the various services offered by associations to their members, such as legal advice, but are not bound to obey the sectoral agreements signed by the association. In turn, they are also not covered by the association’s strike insurance funds and have to bear the costs of industrial conflicts in their plants on their own.

The employer associations developed OT membership categories in response to rising dissatisfaction among members with the results of sector-level bargaining (Haipeter and Schilling 2005: 176-7). They tend to be used, in particular, by firms that are under severe cost pressure and where the strike threat is low. In metalworking about one quarter of all firms are OT members, whereby these firms employ about 10 per cent of all employees (Silvia and Schroeder 2007: 1453). The East German employer associations, confronted with particularly strong member losses (see Table 9.3), have been the pioneers of OT memberships. In many associations in East Germany a majority of members has opted out of sectoral bargaining.

Some associations are even actively encouraging their members to opt out from sectoral bargaining, such as, for instance, the Association of Saxon Metal Employers¹⁵⁵ (VSME), the largest employer association in East Germany (Raess 2006: 462). According to the VSME, only about 4 per cent of the metalworking firms in its region are covered by sectoral agreements, whereby these firms employ 17 per cent of the sectoral workforce (VSME 2007: 1). VSME president Bodo Finger declared in 2007 that “[a]bout 93 per cent of our firms live in a world without sectoral collective agreements and are very successful by doing so, as the growth in turnover, exports and jobs proves” (VSME 2007: 1).

In addition to stopping member exits, employer associations are using bargaining opt-outs also as a tool to put pressure on the unions to moderate their demands, by threatening the unions with a further decline in bargaining coverage in the case of an unsatisfactory agreement. In short, the introduction of OT membership categories is a response by employer associations to growing opposition among some of their members to sectoral bargaining. OT membership has led to a partial decoupling of the organizational self-interests of employer associations from collective bargaining institutions. With the help of OT memberships

¹⁵⁵ According to the VSME, the share of Saxon metalworking and electro-technical firms still covered by the sectoral agreement with the IG Metall was about 4 per cent in 2006, whereby these firms employed about 17 per cent of all sectoral employees (VSME 2007: 1).

employer associations can kill two birds with one stone: they can arrest the hemorrhage of members and, at the same time, increase pressure on unions to make concessions.

9.V Discussion

During the 1990s, German employers became a driving force for institutional transformation. Rather than defending existing institutions and policies against radical reform initiatives, as some arguments predict, they became one of the main protagonists of institutional change in welfare state politics and industrial relations. Dissatisfied with the slow progress of welfare state reform, the priority of employers shifted from participation in consensus-oriented corporatist policy-making towards public campaigning and opinion formation, aimed at welfare state retrenchment and reductions in non-wage labor costs and tax burdens. This constitutes a remarkable change compared to previous decades, when employers to a large extent accepted social policies as an important contribution to social peace. Moreover, large firms often used social policies to facilitate the peaceful shedding of older workers, like long-term unemployment insurance or disability pensions. This practice provided them also with an economic interest in the continuation of this policies. Over time, however, the resulting rise in non-wage labor costs made employers increasingly skeptical towards this practice and contributed to a paradigm shift towards welfare state cost containment. Today, employers' demands for cost-cutting measures include also the systematic closing down of pathways to early retirement (BDA 2009: 13).

Employers did not strive for the outright abolition of the institutions of the German model, the Bismarckian welfare state and the dual system of industrial relations. Instead, they tried to transform the German model from within, a transformation that aimed at outcomes that were more market-oriented and less costly for employers. In contrast to what the VoC approach predicts, the business federations, together with the free market-oriented Free Democrats (FDP), belonged to the most forceful protagonists of market-liberalizing institutional change. There is little empirical evidence of labor market liberalizing or welfare retrenching reform initiatives that employers had opposed. In general, employers welcomed liberalizing reform initiatives, such as the Hartz reforms, but insisted on the need for further-going reform efforts.

Throughout the 1990s, employers' political efforts were single-mindedly focused on reducing non-wage labor costs and tax burdens on business by way of welfare cuts and the general downsizing of public expenditures. These demands imply also greater scope for

market solutions, such as, for instance, the BDA's proposal for mandatory private care insurance and proposals for a greater role of private pensions (see section III above), as well as measures to re-commodify the unemployed by way of making unemployment benefit entitlements more restrictive and tightening the work obligations of the unemployed. In industrial relations, employers pushed for decentralization and deregulation within the existing institutional framework of the dual model. While these demands do clearly not amount to an outright abolition of the institutions of the German model, they nevertheless aim at a substantially more market-oriented political-economic order, with greater divergence in wages and working conditions and a less redistributive welfare state.

The radicalization of employers' reform demands was accompanied by a turn away from the post-war model of social compromise at the political level. While in industrial relations employer associations still tried to achieve reforms by way of negotiations with labor unions and works councils, at the political level they moved away from compromise-oriented policy making. Attempts to forge corporatist compromises on welfare state and labor market reforms through the *Alliance for Jobs* talks that the government initiated were half-hearted and essentially came to naught. Employers welcomed the subsequent shift by the government to unilateral reforms through the Hartz committee and the *Agenda 2010* reform program, which intended to neutralize the unions as veto players. The fact that no compromise between unions and employers in the *Alliance for Jobs* could be found indicates that employers are not content anymore with incremental adjustments to existing policies and institutions, but are instead aiming at more far-reaching reforms. Employers came to realize that these type of reforms could not be achieved by way of social compromise. Instead, they realized that they needed to take more assertive stances and seek political confrontation through public campaigning.

The turn to political confrontation aimed ultimately at changing public opinion and the thinking of elite policy-makers by impressing the importance of market-oriented reforms on them. Through public campaigning and media statements employers consistently pushed the *Standortdebatte*, often relying on exit threats and the challenges of international competition to make their case for market-oriented and cost-cutting reforms. This reflects a new political strategy, one which differs from the strategy of political accommodation of the post-war period. Rather than relying solely on negotiations and participation in corporatist decision-making, employers increasingly tried to shape public debate in order to ease political constraints in the electoral arena. Employers came to realize that electoral support for 'big government' constituted a major constraint on the kind of market-oriented reforms they were

aiming at. Easing these constraints could not be achieved by way of seeking political compromises with other actors, but required an effort to change public opinion.

The radicalization in employer positions and strategies was fuelled by conflicts between small and large firms. Smaller firms typically have fewer capacities to deal with rising competitive pressures and do, therefore, consider the constraints imposed by collective bargaining and welfare state programmes more of a burden than larger firms. Moreover, they have also fewer opportunities to make use of social policies to facilitate peaceful labor shedding. While in the past big industry tended to dominate decision-making within the employer associations, the increasing dissatisfaction of smaller firms required the associations also to pay more attention to their smaller members. This is most evident in the field of collective bargaining. During the 1990s, small firms tended to leave sectoral bargaining institutions. Large firms, in contrast, tended to remain loyal to sectoral bargaining and push for decentralization and flexibilization within the existing institutional framework. Under pressure from dissatisfied smaller members, the employer associations decided to introduce bargaining opt-outs, which, in effect, facilitated the further erosion of sectoral bargaining. Rather than defending sectoral bargaining institutions, in which they clearly have an organizational self-interest, the employer associations had thus to accept their erosion.

Conclusions

During the 1990s, German employers became increasingly dissatisfied with important components of the German model, in particular the size of the welfare state and the regulatory constraints created by sectoral bargaining. Rather than defending existing institutions and policies against deregulatory reform initiatives, they turned into protagonists of such reforms. This change in employer politics took several forms. First, it took the form of an intensification of opinion formation efforts and public campaigning in favor of market-liberalizing and cost-cutting reforms, underpinned by the so-called *Standortdebatte*. Second, employers tended to withdraw from institutions of social compromise at the political level. Government attempts to forge corporatist reform compromises through the *Alliance for Jobs*, for instance, come to naught, in part because employers' confidence in social compromise had eroded and negotiations had therefore been half-hearted.

Third, in industrial relations, employer associations still relied on institutions of social compromise, but many smaller firms tended to defect from it, either by leaving sectoral bargaining or by not complying with agreements, leading to the shrinking of the German

model of industrial relations. The emergence of internal differences between small and large firms contributed to the associations' turn away from political accommodation and forced them to pay closer attention to member interests. Under pressure in particular from smaller members the employer associations introduced bargaining opt-outs and tried to decentralize collective bargaining functions. Both measures did, in effect, contribute to an erosion of the sectoral bargaining model, rather than bolstering it. These changes do clearly not aim at the outright dismantling of the existing welfare state and industrial relations institutions, but nevertheless at a considerably more liberal political-economic order, with a less redistributive welfare state and less restrictive regulations of wages and working conditions.

I have argued that this change in employer politics resulted from the interaction of international and domestic changes. Intensified competitive pressures, caused by globalization, met with a domestic reform deadlock, caused by the electoral popularity of existing policies. Global competition made employers prioritize labor cost reductions more than in the past, while at the same time paths to cost-cutting welfare retrenchment appeared to be blocked for political reasons. The concessions that social compromise required from employers came, therefore, to be increasingly at odds with what they thought to be able to afford in the context of global competition. At the same time, and different from the post-war period, employers could now afford to subordinate their interest in social peace to their interest in lower labor costs. Their heightened ability in a globalized economy to rely on credible exit threats resulted in a more accommodationist approach by labor and meant that employers had to rely less on political accommodation themselves. Through plant-level "employment pacts", for instance, employers could gain concessions from labor, without jeopardizing social peace.

The findings in this chapter put into question arguments that see German employers as active defenders of the existing labor market and welfare state institutions. Rather than fighting against reform initiatives by other actors, employers have themselves become protagonists of reform. To the extent that German firms perceive institutions and policies to be in their genuine interest, we should expect them to oppose reforms that retrench or transform these policies and institutions. However, there is little evidence of market-oriented or deregulatory reform initiatives that employers had opposed. In general, employers have become protagonists of market-oriented reforms, rather than defenders of the existing system. This constitutes a remarkable change to the post-war period, during which employers largely accepted existing institutions and policies as a necessary contribution to social peace. The interaction of domestic and international changes resulted in a change in employer priorities:

Social peace became much easier to maintain in a globalized economy, while the rise in labor costs, which was created in part by past policies to support social peace and their intensified usage, raised the price employers had to pay. Consequently, their priorities shifted from policies securing social peace to cost containment and welfare retrenchment.

10 Conclusions

In capitalist societies capital possesses structural power due to its control over investments and production. How did capitalist societies manage to construct institutions that constrain capital's control over economic outcomes given capital's structural power? There are in principle two possible basic answers to this question. The conventional *balance of class power* argument explains this fact with the political strength of the labor movement and its parliamentary allies and its capacity to mobilize enough political power resources to compensate for the structural power of capital (Korpi 1983; Huber and Stephens 2001). While this has for some time been the dominant explanatory approach to welfare state development, since the 1990s it has been increasingly challenged by a new approach that argues that the successful construction of market-correcting policies and institutions was not so much the result of labor power subduing capital power, but was, instead, promoted by capital itself, thus questioning the explanatory relevance of the labor power argument. This later argument has become known as the cross-class coalition thesis. Isabela Mares, one of the protagonists of this new argument, claims that “[u]nder some conditions, firms support the enactment of a new social policy, not out of altruism or generosity, but out of self-interest” (Mares 2003a: 250). In this view, market-correcting policies reflect not the weakness, but the strength of capital interests.

The argument put forward in thesis has challenged the cross-class coalition thesis on empirical and theoretical grounds. The cross-class coalition argument has some *prima facie* plausibility given that employer associations, the representatives of capital interests in the domain of social and labor market policies, have historically often consented to specific social policies. As this thesis has shown, employers have in general neither actively advocated market-correcting social and labor market policies nor adamantly opposed them. Instead, they have often accepted specific reform proposals that have been put on the agenda by other actors. The cross-class coalition argument, however, misspecifies the preferences of employers, that is, it misinterprets the reasons why employers have consented to these reforms and thereby misunderstands the causal role of employer behavior in welfare state development. This concluding chapter highlights the main findings and themes of this thesis and tries to strengthen the argument that employer's consent to welfare state expansion

reflects an accommodation to political constraints rather than a genuine preference for social policies rooted in economic interests.

The cross-class coalition thesis suggests that employers' consent to the formation of welfare state policies reflected genuine economic interests. In her study, Mares, for instance, identifies the interests of firms in skill formation and the redistribution of social risks across different categories of firms as the most important factors explaining the support of specific groups of employers for social and labor market policies (Mares 2003a: 249-255). This thesis has put forward an alternative explanation, which highlights political motivations and political context as crucial factors explaining employers' consent to welfare state policies. Employers have consented to welfare state policies not because they wanted to design an institutional and policy framework that is beneficial to economic production and labor productivity but because they realized that the alternatives on the agenda would have constrained entrepreneurial freedom even more. This fact has important theoretical implications because it puts into question the independent causal role of employers as promoters of welfare state development. Consequently, the role of employers in welfare state development cannot be understood appropriately without taking into account the historical political context within which they have made their choices.

The thesis has highlighted, in particular, two types of motivations for employers to consent to welfare state and industrial relations policies. First, a political interest in defeating challenges to the existing capitalist order and industrialists' control over production, which led to a *politics of pacification* that involved concessions to labor on social and labor market policy issues. Second, an interest in maintaining influence on government elites in the policy-making process has compelled employers to cooperate in the planning of reforms, when they perceived the chances of stopping a reform project entirely as weak. This is what I call the *politics of containment*. Politics of containment aims at limiting the negative impact of new social policies on firms, most notably in terms of labor costs. In contrast to outright opposition to a planned policy, cooperation promised the prospect of influencing important details of planned reform projects in the interest of employers. Cooperation presupposes the acceptance of the basic political goals of reformers. The importance of these two goals and strategies, pacification and containment, made the formation of cross-class alliances difficult, as these goals diverged from those of labor.

Table 10.1 Summary of Employer Goals in Key Reform Projects

Bismarck's social reforms	<ul style="list-style-type: none"> - social pacification to stabilize the existing political-economic order - suppressing labor unions and social democracy - overcoming a disliked policy legacy (employers' liability legislation) - limiting cost impact of planned reforms on industry
Collective bargaining before World War I	<ul style="list-style-type: none"> - preventing strikes where suppressing organized labor not possible - limiting wage competition
Stinnes-Legien agreement	<ul style="list-style-type: none"> - social pacification to prevent social revolution and collectivization * - ensure orderly economic demobilization - retraction of concessions once political situation stabilized
1927 Unemployment Insurance	<ul style="list-style-type: none"> - improving work incentives by overcoming unfavorable policy legacy (unemployment assistance) - influencing relevant details of an unstoppable reform by cooperating in the policy-making process - ensuring employer influence in the governance of the new programme
1945/1948 social insurance reforms	<ul style="list-style-type: none"> - opposition to a shift from a Bismarckian to a universal social insurance system - no "politics of containment" necessary as no political majority for this reform
1950/1951 Codetermination Laws	<ul style="list-style-type: none"> - strong opposition to parity codetermination - reluctant cooperation in policy-making under pressure by Adenauer - no politics of containment / employers lost
1957 Pension reform	<ul style="list-style-type: none"> - cost containment - drafting of alternative plan to limit cost effects - politics of containment unsuccessful / employers lost
1990s social policy	<ul style="list-style-type: none"> - Cost containment through public campaigning - Turn away from social compromise and accommodation
1990s industrial relations	<ul style="list-style-type: none"> - Decentralization and flexibilisation through negotiations with unions - Collective bargaining exit by smaller firms

Source: own elaboration

The thesis has linked these two types of motivations, pacification and accommodation, to historical periodisation, whereby the goals of employers changed with the changes in the political challenges they faced. The thesis has found that, initially, in the Wilhelmine Empire

and in the aftermath of World War I, social pacification had been the dominant motivation for industrial employers to consent to social and labor market policies. With the transformation of the labor movement from a revolutionary to a reformist force, containing planned reform initiatives became the dominant goal of employers. Social pacification receded into the background, but remained a relevant consideration. The table below summarizes the main goals pursued by industrial employers in the individual reform projects analyzed in this thesis.

10.I Employers' Politics of Pacification

Bismarck's social reforms in the 1880s and the Stinnes-Legien agreement, signed in 1918, are the two reforms that were shaped most clearly by the *politics of pacification*. In both cases, industry used social pacification as a tool to try to maintain its powerful position in society. The introduction of social insurance by Bismarck resulted from an alliance between the state elites and the politically influential heavy industry. Both perceived the emerging social democratic labor movement as a revolutionary threat. The authoritarian "master in my own house" standpoint dominated within heavy industry, which was the dominant sector of industry during the Wilhelmine Empire (1871-1918). The heavy industry was opposed to granting workers any participation rights, whether within the firm or in politics, and resorted to occupational social benefits to pacify workers. It is thus no coincidence that support for social insurance was strongest in that sector of industry that was also most hostile to the emerging socialist labor movement. Support for social insurance appears to have been more fragmented in the manufacturing industries, which were more willing to recognize labor unions, but these sectors were still very small during the 1880s.

The salience of social pacification to heavy industry was amplified by the existing employers' liability legislation for work injuries. This liability legislation contributed to the aggravation of class conflicts and had fuelled the labor movement because it required injured workers to go to court against their employer to gain compensation for injuries. Heavy industry, where the incidence of work injuries was high, had a particular interest in replacing employers' liability obligations with a public work injury insurance scheme, which promised to eliminate an important source of class conflict and union agitation by shifting responsibility for compensation to the state. Political lobbying by the heavy industry focused thus also primarily on the issue of work injury insurance, and much less on the other programmes initiated by the government (health insurance and disability and old-age pensions).

Work injury insurance was, in fact, one of the very few social policy programmes in the history of German welfare state development whose introduction was actively promoted by industrial employers, rather than merely accepted. In a highly exceptional way, industry had acted as an agenda-setter in the case of work injury insurance. All other major reforms had been put on the agenda by other political actors, and not by industry. This “outlier” position is explained by the problematic effects of the existing liability law for industrial employers. This law was generally considered inadequate by all major political actors. The alternative to work injury insurance that was on the political agenda, advocated by the social democrats and part of the state elites, consisted of a tightening of liability laws and new rules concerning worker protection. This alternative programme, though also informed by a strategy of social pacification, was adamantly opposed by the heavy industry as an unacceptable interference in the internal organization of firms. Industry’s strong opposition to worker protection laws also indicates that its support for work injury insurance was not motivated by a concern for labor productivity, which is clearly harmed by work injuries, but by the conflict-ridden practice of liability lawsuits that resulted from the existing liability law.

Bismarck’s social reforms are neither well explained by the labor power thesis nor by the cross-class coalition thesis. The political strength of the labor movement during the 1880s was still relatively weak, compared to later periods. Anti-socialist laws kept the social democrats weak. In 1887, the SPD gained only 10 per cent of the votes and held 2.8 per cent of the seats in the national parliament (DHM 2008). Social democrats and labor unions were not involved in the policy-making process. The heavy industry was politically powerful and formed a close alliance with Bismarck and the state elites. Industrialists controlled labor relations in their firms unrestrained by state regulations or unions. The government’s turn to trade protectionism in 1879 shielded the German heavy industry from international competition. Domestically, the formation of large cartels and production syndicates prevented competition. The political and economic power of the heavy industry was arguably at an all-time high in the 1880s. Bismarck’s social reforms were thus neither the result of objective changes in the balance of class power, nor were they the straightforward result of the material interests of capitalists.

Instead, the introduction of social insurance was the product of conservative social reformers within the government bureaucracy, who were supported by dominant groups of industrialists. Their paramount motivation was to defend the existing power structure and prevent a social revolution by suppressing the socialist labor movement. What motivated the

Bismarckian social reforms was not so much the objective political strength of the labor movement, but rather its perceived threat to the existing political-economic order. The granting of social rights to workers was intended to prevent them from claiming political rights. The cross-class coalition thesis is thus right when claiming that dominant groups of German industrialists had supported the introduction of social insurance, but it misrepresents the preferences behind their support. Social pacification and consolidation of power, rather than managerial interests in skill formation and labor productivity, were the underlying preferences.

Social pacification again motivated concessions by industry to labor after World War I. Defeated in the war, the Wilhelmine Empire collapsed in November 1918 and industrialists were confronted with the threat of an imminent social revolution by a worker movement that was inspired by the Soviet revolution in Russia one year before. An agreement signed between major industrialists and moderate labor union leaders in November 1918 included far-reaching concessions to labor, such as the eight-hour working day, recognition of labor unions, sectoral collective bargaining, works councils and parity-based arbitration bodies. This agreement became known as the Stinnes-Legien agreement.

The character of social pacification in the Stinnes-Legien agreement differed from the introduction of social insurance in the 1880s. While during the 1880s, social pacification was directed against the socialist labor movement as such, the Stinnes-Legien agreement was directed more narrowly against revolutionary elements within it. Under the impression of the revolutionary threat, industrialists now, for the first time, cooperated politically with union leaders, including both social democratic and Christian democratic union leaders. At the same time, the role of the state had changed fundamentally. While during the 1880s, social pacification was the result of an alliance between a conservative state elite and industry, now, as the old regime had collapsed, industry could not rely on its old ally anymore. Instead, industry now turned to moderate labor union leaders for help against radicalized elements within the labor movement. The kind of concessions offered to labor now had to be different: to gain the cooperation of the labor unions, social benefits were not enough. What were now needed, instead, were participation rights for the labor unions (Reichert 1919).

The shift in the types of concessions offered in turn for social pacification also reflects the changes in the sectoral composition of German industry. The rise of the more liberal manufacturing industries since the late 19th century onwards had begun to challenge the political leadership role of the conservative heavy industry. For the heavy industrialists any form of cooperation with labor unions had always been an absolute no-no. In contrast, some

other sectors (construction, printing and timber, in particular) had already started to bargain with unions before World War I. As shown in chapter 2, these differences resulted primarily from sectoral differences in union strength and vulnerability to strike action. The leading protagonists behind the Stinnes-Legien agreement came from the manufacturing industries, rather than from the heavy industry. Significant opposition to the Stinnes-Legien agreement existed within industry and contributed to the collapse of cross-class cooperation a few years later, when the political situation had stabilized. It is also noteworthy that the agreement was initiated by a group of individual industrialists, and not by their associations. The two peak-level industry federations (CDI and BdI) opposed the agreement (Feldman 1976: 339).

The establishment of institutions of social compromise and cooperation by the Stinnes-Legien agreement was not the result of far-sighted employers trying to design policies and institutions more attuned to the needs of industrial production. It was, instead, an *ad hoc* response to the political uncertainty that characterized that historical moment. Some scholars have emphasized the dependence of German industry on specific skills as a reason for German industry's support for the introduction of institutions of social compromise during this period. Gerald Feldman, for instance, has argued that the revolutionary situation in 1918 merely brought about institutional changes that would have been unavoidable anyway given the structural shift in the German business community to the more progressive manufacturing sectors (Feldman 1976: 393-40). Cusack, Iversen and Soskice¹⁵⁶ use the Stinnes-Legien agreement as an example to illustrate their argument that inclusionary institutions were adopted to protect investments in so-called co-specific skills (Cusack et al. 2007: 380). While it is correct that the manufacturing industries relied more on skilled labor than the heavy industry, the archival evidence does not provide any indications that the issue of skill formation played a significant role in industry's deliberations leading to the agreement (see chapter 4). Moreover, the collapse of class cooperation only a few years later speaks against the hypothesis of far-sighted industrialists trying to modernize the production regime.

The Stinnes-Legien agreement is one of the rare cases of a cross-class alliance in the development of the German political economy. It was an alliance between moderate forces on both sides of the class divide and was directed against revolutionary forces within the working class. It was united by the joint goal of preventing a Soviet-type revolution under the control of the so-called "worker councilor movement" (*Rätebewegung*).¹⁵⁷ Employers made far-reaching concessions to the labor unions to ensure their cooperation in an orderly

¹⁵⁶ Building on work by Kathleen Thelen (Thelen 2004)

¹⁵⁷ This movement should not be confused with the institution of works councils within firms.

transition to a new political-economic order. This alliance was a historically contingent event that resulted from the extraordinary political and economic uncertainty that characterized the aftermath to World War I. Through collaboration with organized labor, industrialists expected to be able to reduce the uncertainty over the future development of Germany and prevent the collectivization of industry. The revolutionary situation had changed the options available to industry. Before the war, industry could rely on the state to secure a non-interventionist regime and had thus little need for political collaboration with labor. The revolutionary situation had changed that. The alliance was the result of a strategic accommodation of industrialists to a highly unfavorable context. Their acceptance of labor-inclusionary institutions, including works councils and parity-based arbitration committees, did not reflect genuine preferences for these institutions but was part of the strategic accommodation.

10.II Employers' Politics of Containment

A second reason why employers accepted specific social policies, in addition to their genuine preference for social pacification, is strategic: to support specific proposals in order to prevent other proposals that were also on the agenda from being chosen. Support for such proposals reflects lower-order preferences, that is, preferences for “lesser evil” outcomes. These preferences become the positions taken when the first order preference is realistically not available. Employers have often consented to specific reforms relatively late in the policy-making process, when it became clear that the passing of the policy could not be prevented entirely. If this situation occurred, employers often decided to support the policy and cooperate in the drafting of the legislation in order to be able to influence important details in the interest of industry.

The process leading to the introduction of unemployment insurance is a clear case in point. The national employer federation (VDA) had consented to the introduction of unemployment insurance in 1927. This decision did not, however, result from a genuine preference for unemployment insurance, but was an adjustment to a changing political context. Employers' support for unemployment insurance had not been clear-cut and consistent but had instead been wavering. In the Wilhelmine empire, when there was a clear parliamentary majority against unemployment insurance, employers had also been strongly opposed to unemployment insurance. Their key concern had been the suspected effects of unemployment insurance on work incentives. Unemployment insurance creates a reservation wage and was, for this reason, expected by industry to harm work incentives and reward the idle “work shirkers”.

After the war the situation had changed in two respects. First, a political majority in favor of unemployment insurance had begun to materialize in the Weimar Republic. Continued opposition by employers threatened to undermine their influence in the policy-making process. Participation in policy deliberations and negotiations allowed them to voice preferences over details they were particularly concerned about in a way that fundamental opposition would not have allowed to. Second, the introduction of the programme of unemployment assistance in 1918 had changed the policy status quo in an unfavorable way. Unemployment assistance was a means-tested and flat-rate benefit, and was administrated by the municipalities. Employers had no control over who would receive unemployment assistance benefits and due to its universal, flat-rate character the programme harmed work incentives even more than unemployment insurance. Unemployment insurance, in contrast, was perceived as less harmful in terms of work incentives, because it is based on previous employment and earnings-related benefits, and does thus not threaten to benefit the so-called “work shirkers.” In addition, unemployment insurance gave employers a greater say over the usage of funds, as employers would be involved in the administration of the programme.

Strategic accommodation played a role in most instances of reform analyzed in this thesis, as employers were hardly ever able to get things their way completely. Even in the case of Bismarck’s social reforms strategic motivations played an important role. As mentioned above, dominant groups of industry did genuinely believe that the social insurance project would be necessary to pacify the working class. Thus, their support for social insurance was based on a genuine interest in social pacification. Nevertheless, industry’s decision to cooperate in the drafting of the social insurance legislation was also, in addition, motivated by strategic concerns of being able to influence important details of the planned reforms. One industry representative candidly remarked about a specific policy aspect that “resistance by industry would be to no avail, because the current general mood is now against industry, one would simply decide by ignoring industry” (Beutner in Baare 1880: 55, translated by TP). The overall goal of industry’s cooperation was to thereby make sure that benefit levels would be kept as low as possible and to limit increases in labor costs. Industry did however perceive its strategy of influence via cooperation as not sufficiently effective and did, over time, become more reluctant to go along with Bismarck’s plans (see also chapter 3.III).

Industry also sought to contain social policy expansion by presenting alternative proposals, in situations where the political debate moved into a direction unfavorable to

industry. Such proposals often had the character of a compromise between industry's own preferences and other proposals on the agenda. A characteristic case in point is the so-called "dynamisation" of pension benefits in 1957. This reform included the automatic indexation of pensions to gross wage development, something that was firmly opposed by industry. The BDA presented an alternative proposal that was based on discretionary pension increases based on decisions by an expert committee. This proposal did not, however, succeed (see chapter 7, section III).

A similar example is provided by the introduction of public long-term care insurance in 1994. This reform was also strongly opposed by industry because of its effects on labor costs. Relatively late in the policy-making process, the BDA came up with its own alternative proposal for long-term care insurance. This proposal consisted of mandatory private insurance on a pre-funded basis for most of the population. The BDA model did not succeed in this case either. These examples show that proposals launched by employer associations often do not reflect their genuine preferences, but their strategic calculations of which policy option has the highest chances of success in a given situation. Employers' support for specific policy options cannot be taken as evidence for the proposition that employers had been active supporters of social policy expansion. Even when their policy proposals had been expansionary, as in the two examples mentioned above, their intention had been to limit social policy expansion. When they made such expansionary social policy proposals, they often did so in the face of proposals of other actors that were even more expansionary, and not because of a genuine preference for expansion.

In addition to accommodating to the policy choices on the agenda, German employers have also often changed their policy positions in response to the introduction of new policies. New policies alter the policy status quo, the set of existing policies, against which employers need to evaluate the value of any alternative policy option. The case of unemployment insurance discussed above illustrates this point. Before the introduction of unemployment assistance industry did strongly oppose unemployment insurance. The introduction of unemployment assistance had weakened resistance among employers to unemployment insurance, because unemployment assistance turned the policy status quo more unfavorable to employers. Similarly, industry's promotion of work injury insurance in 1880/81 resulted primarily from the problems created by the old liability legislation, introduced in 1871, and the aggravation of class conflicts that it was perceived to have fuelled. Changes in the policy status quo can thus also change the policy goals pursued by political actors.

Employers' choice for strategic accommodation to the political situation results from the necessity of their associations to strike a balance between the preferences of their members and their interest in gaining and cultivating political influence, most importantly through contacts to the government bureaucracy. Their publicly taken positions can thus not be taken as an accurate representation of their underlying genuine preferences, but need to be seen in the political context. Philip Schmitter and Wolfgang Streeck have coined the concepts *logic of membership* and *logic of influence* to capture this tension between representing member interests and exercising influence (Schmitter and Streeck 1981). As these two authors argue, business interest groups need to take into account both logics in order to be effective mediators between their members and the political system. Influence requires cooperation with interlocutors, which requires a certain accommodation to the interlocutor's goals. For this reason it is important to be cautious about inferring genuine preferences from observable political behavior. If an actor's support for a specific policy is strategic than the support is endogenous to the policy-making process and can thus not serve as the principal component of a causal explanation of that policy.

10.III Codetermination: The Limits to Pacification and Accommodation

In all but one of the policy cases analyzed in this thesis did employers accommodate their policy demands to the political context. This one exception is co-determination. It is therefore important to compare this case with the other cases and look what made codetermination different.

Employers had adamantly opposed the introduction of parity co-determination in the early post-war period, even at the clear risk of being defeated. They did not offer concessions, as the strategic accommodation thesis allows us to predict, but did instead decide to openly fight the introduction of codetermination. Only reluctantly, and under strong pressure from Chancellor Adenauer, did employer representatives in 1950/51 consent to take part in negotiations leading to the institutionalization of parity codetermination in the heavy industry. Industry and its parliamentary allies managed to prevent the extension of parity codetermination to sectors outside the heavy industry, which became instead governed by a weaker form of codetermination that was acceptable to industry. Even after the passing of the codetermination laws (1951/52) industry continued to campaign strongly against codetermination, though, in practice, most firms did comply with the laws and did not obstruct their implementation. In the 1970s, the BDA challenged the constitutionality of

codetermination in court, indicating the continued salience of the issue to industry (see Chapter 8.II).

The case of codetermination indicates the limits of social pacification and strategic accommodation. As shown in chapter eight, industrial employers considered labor union demands for parity co-determination as an attack on private capital ownership. For industrialists, 'economic democracy' constituted a piecemeal programme intended to lead to collectivization and a centrally planned economy under the control of union functionaries. Co-determination was perceived as communism in disguise, so to speak. In particular, industry feared to lose control over investments and a shift in the balance of power to the labor unions, as unionists would also function as labor representatives in supervisory boards. Through their centralized organization, unions would be able to use codetermination as a tool for centralized economic planning, effectively disenfranchising the individual industrialist of his ownership rights, so the suspicion. For these reasons, the issue of co-determination was not amenable to a strategy of social pacification. Indeed, defeating challenges to entrepreneurial freedom and private capital ownership were precisely the goals of social pacification. Social policies were the means, the protection of entrepreneurial freedom and private capital ownership the ends. Industry's willingness towards compromise and pacification ended, where entrepreneurial freedom and private capital ownership themselves appeared to be at stake.

The case of codetermination provides us with important information concerning the ultimate motives that informed employers' consent to social policies, that is, the genuine preferences that underlay their behavior. Why did employers often consent to compromises on social policy issues, while they were reluctant to do so with respect to codetermination? Clearly, compromise is not an end in itself. Actors will only consent to a compromise if thereby they can satisfy their genuine preferences in a better way than otherwise. If the essence of a proposal is in direct opposition to an actor's genuine preferences no compromise will be possible.

In the field of social policy, employers consented to compromises, where this appeared to further their ultimate goals, to defend private capital ownership and entrepreneurial freedom. Social policies and collective bargaining may raise labor costs, but they do not intervene with capital ownership rights, the rights of capital to decide unilaterally over investments and the use of profits. Social policies were thus, in principle, an appropriate tool of social pacification during those historical moments when capital ownership rights appeared to be at risk. Co-determination, in contrast, infringes capital ownership rights by partially

shifting these rights to the representatives of labor. Therefore, there was no point for employers to make concessions on codetermination to labor, as this would not have helped them to further their ultimate goals. Moreover, there was also little risk of a more radical solution through unilateral government action, as the CDU-led coalition government was generally skeptical about codetermination.¹⁵⁸ Open confrontation against labor was thus the best option available to employers.

German industry's alternative to co-determination and economic planning was the "social market economy". The social market economy was an ideological template for the organization of the economy that was intended to give political legitimacy to an economic order based on free markets and private capital ownership. Although the content of the concept had been defined only vaguely by its protagonists, an emphasis on free market competition had always been put at the center by its protagonists. As shown in chapter six, the concept was developed and used by its protagonists, including business, as an ideological tool to emphasize the normative superiority of economic liberalism over its main rivals, which were understood to be communism in the East and "economic democracy" in West Germany. The concept of social market economy was thus marshaled against codetermination, which further indicates the strength of industry's preferences against codetermination.

10.IV Employers and the Conservative Welfare State

It would be easy to conclude from the fact that employers had often accommodated their positions to the political context that employers had little causal impact on welfare state development. As shown in this thesis, they have very rarely been part of alliances promoting the expansion of social policies. Neither have they been fighting adamantly against social policies per se. They have, by and large, responded to policy initiatives coming from other actors by trying to influence policy details in the direction they preferred. This raises the question in what way and in which direction employers have shaped German welfare state development. Did employers leave an imprint on German welfare state development? In which direction did they influence the policies and institutions of the welfare state and industrial relations? What types of social policies did employers support and which ones did they try to prevent?

I have argued in this thesis that employers have supported social policies not because they thought that they would be in their economic interest, but because constraints created by

¹⁵⁸ An exception to this was the CDU labor wing, which did support co-determination.

the political environment often turned these policies into the lesser of several evils. Most likely, in the absence of challenges to private capital ownership and strong pro-welfare forces employers would not have supported any social policies at all. This argument, however, is not intended to imply that employers did not care about the characteristics of the policies they supported, as long as the supported policy served its purpose of preventing the “greater evil”. Employers genuinely preferred social policies over others.¹⁵⁹ For employers, not all social policies were of equal value, despite the fact that they did not necessarily hold a genuine preference for any of them. Hence, once consideration of the political context had convinced employers that supporting a specific policy is the best of the choices available, they tried to shape the details of that policy in line with their more specific policy preferences.

The findings in this thesis show that German employers have consistently favored those types of social policies that follow the characteristics of what Titmuss termed the “industrial achievement” model (1958) or what Esping-Andersen termed conservative social policy (Esping-Andersen 1990: 58-69). Titmuss distinguished between three different welfare state models, the industrial achievement model, the residual welfare model and the institutional-redistributive model. Building on Titmuss, Esping-Andersen typologises social policies into conservative, liberal and social democratic (or universalistic) policies. Of these three types of social policies, employers’ support focused on those policies that followed the conservative or industrial achievement model. This means that they have consistently preferred policy programmes based on earnings-related benefits to programmes based on universal benefit entitlements or means-testing. They preferred programmes that provided benefits based on employment and past earnings, financed by contributions from employers and employees and with some control by employers over the administration of these programmes. They opposed programmes providing universal benefits, independent of previous employment, or administered directly by the state without any participation by employers.¹⁶⁰

Employers’ support for the conservative social policy model appears to have been motivated by a set of preferences. Most importantly, social insurance appeared to provide advantages compared to other types of social policy in terms of *work incentives*. By work incentives I mean incentives for individuals to accept work as well as to perform well at work (work effort). Work incentives and worker motivation were important concerns that shaped

¹⁵⁹ In this respect, this thesis is in line with the cross-class coalition thesis, as shown below.

¹⁶⁰ To clarify, employers’ positions were not the principal reason why Germany embarked on the path of conservative welfare state development. Other actors, such as the bourgeois social reform movement in academia, government officials and the Christian Democratic labor movement also made important contributions to set Germany on the path of a conservative welfare state.

employers' positions on social policy issues. In short, employers were concerned that social benefits will make workers independent from work, will thus undermine work incentives and, consequently, reduce labor supply and work effort. As shown in chapters three and five, the issue of work incentives played a key role, in particular, in the introduction of old-age and disability pensions in 1889 and the introduction of unemployment insurance in 1927. Social insurance schemes offered some advantages in this respect compared to other types of social policy programmes, because they provide benefit entitlements on the basis of previous earnings. The decommodifying character of social insurance programmes is thus more limited compared to universal or residual benefit programmes (Esping-Andersen 1990: 23). By linking benefits to past earnings and past employment they make sure that workers remain dependent on employment and work incentives are not eliminated.

Work incentives also explain the variation in employers' support for the various social insurance schemes. The intensity of employers' support was strongest in the case of work injury insurance, followed by health insurance, then disability and old-age pension insurance, and finally, unemployment insurance, the programme most reluctantly endorsed by employers (see chapters 3 and 5). This variation is due to the differences in the extent that these four programmes offer opportunities for benefit abuse by "work shirkers." Work injury insurance did not give rise to concerns over benefit abuse because the occurrence of the risk can be easily monitored. The issue of benefit abuse also did not play a major role in the case of health insurance. Employers were more reluctant to go along with Bismarck's plans for a public disability pension system and justified their skepticism with the argument that disability insurance would be prone to abuse by work shirkers (see chapter 3.III).

Unemployment insurance was the last of the four social insurance schemes introduced and was also the one that met with the greatest opposition from employers. Unlike the other social insurance schemes, unemployment insurance provides benefits to persons that are assumed to be, in principle, capable and available to work. Employers perceived unemployment insurance to be particularly prone to benefit abuse because the status of unemployment is not linked to any easily observable characteristic, such as age, injury or sickness. Thus the problem of undermining work incentives and promoting work dodging was greatest in the case of unemployment insurance. Employers' evaluation of unemployment insurance changed, once the introduction of the universal unemployment assistance programme led to a policy status quo that appeared to undermine work incentives even more.

By linking benefits to past earnings, social insurance programmes consolidate the market outcome of wages. Employers could thus present social insurance benefits as a deferred wage, something the worker has earned an entitlement to due to his work effort. Earnings-related benefits provide an additional reward to the worker that, presumably, is proportional to his performance at work and thus may benefit his motivation at work. For the same reason, employers have always strongly opposed redistributive elements in social policies. To gain the comparative advantages of the social insurance model employers were ready to contribute to the financing of social insurance. Financing of social insurance programmes by contributions from employers and employees was always in principle accepted by employers.

Employers did, over time, become more concerned about the increases in labor costs caused by the growth in social expenditures. Through a politics of containment they tried to limit the further growth in social expenditures. They lobbied for benefit levels and entitlement criteria to be defined as restrictive as possible and tried to prevent the further expansion of social insurance programmes, for instance by trying to prevent the inclusion of additional social groups. This behavior can be discerned already as early as in the 1890s (see e.g. Büren 1934). The participation of employers in the drafting of unemployment insurance in the 1920s, for instance, was motivated, *inter alia*, also by the intention to make sure that an increase in labor costs would not occur. Similarly, employers' opposition to the so-called "dynamisation" of pension benefits in the 1950s was also motivated by fears of rising social expenditures.

From the 1990s onwards, the importance of the labor cost issue to employers increased considerably. A secular rise of social expenditures in recent decades made employers increasingly reluctant to go along with a politics of social compromise, like they did in the post-war decades, and contributed to a turn to public campaigning by employers. A key conflict in this respect was the introduction of long-term care insurance in 1994, which employers strongly lobbied against, though they failed to prevent it. Employers have also funded several public campaign initiatives to promote welfare retrenchments, such as the Initiative New Social Market Economy. In all their campaigning for cost containment, German employers did throughout history remain loyal to the conservative/industrial achievement model, with payroll tax financing and earnings-related benefits. They focused their demands on cuts in benefit generosity, rather than on changes in the mode of financing. They did also not advocate a wholesale shift to a residual/liberal welfare state model.

Employers continued support for a payroll tax-financed conservative social policy model indicates that the issue of work incentives is of continued relevance to employers.

10.V Political vs. Economic Interests in Explaining Employers' Choices

If the political accommodation thesis is correct that political constraints, rather than economic interests, motivated employers to accept social policies, how is it then possible that employers have over such a prolonged period of time consistently preferred conservative social policies to liberal or social democratic policies? How does their interest in securing work incentives relate to the political goals that motivated their acceptance of social policies?

To understand this issue it is important to distinguish analytically between (a) the reasons why employers accepted the formation of social policies from (b) their preferences over specific types of social policies. The latter is secondary to the former. The reasons why employers had accepted social protection need to be seen as distinct from the sources of their preference rankings over specific social policy options. Social pacification and political accommodation were the ultimate motivations for employers to accept the formation of the welfare state and industrial relations institutions. Only after employers had decided that the political circumstances required social pacification or political accommodation, preferences over specific policy options came into play.

To illustrate the importance of distinguishing analytically between these two distinct processes of preference formation, take a simple example: Assume we ask a prison inmate to tell us in which prison he would like to serve his prison sentence. The inmate informs us that he prefers prison P1 to prison P2, and prison P2 to prison P3. Let us assume that the inmate does indeed serve his sentence in prison P1. We can then infer that he does so because he has stated a preference for this specific prison. However, the fact that we know in which specific prison he prefers to serve his sentence does not allow us to make any inferences about why he is *in prison*. It would clearly be a logical fallacy to infer that he is in prison because he has stated a preference for being in prison (...or, in prison P1, just for the sake of empirical accuracy).

This example intends to illustrate two related points. First, the question of why the inmate is in prison and why he is in a *specific* prison are analytically distinct questions. The two questions require *different* explanations. Similarly, the question why a political actor supported social protection and why it supported a specific type of social protection should be treated as analytically distinct. Second, if external constraints are ignored a *stated* preference

can easily appear as a *genuine* preference and thus, by inference, as the principal causal factor for the outcome to be explained. In reality, though, the stated preference may as well be a strategic accommodation to political constraints.

The example above helps to demonstrate the differences between the cross-class coalition thesis and the political accommodation thesis. As shown in the introduction chapter (chapter 1), the cross-class coalition thesis rests on an economic-functionalist logic, while the political accommodation thesis rests on a political-strategic logic. Research by proponents of the cross-class coalition thesis (e.g. Mares 2003b; Swenson 2002) tends to assume that employers' support for specific policies reflected their genuinely held preferences, rooted in objective economic interests, such as interests in skill investments (Mares 2003a: 29). Thus, the cross-class coalition thesis suggests, employers' structural power and pro-welfare preferences were an important causal force behind welfare state formation and expansion. In contrast, the political accommodation thesis suggests that employers' acceptance of welfare state formation reflects a choice for a lesser evil, resulting from the accommodation to an unfavorable political context. In theoretical terms this difference can be expressed in the form of two alternative preference rankings, which are shown in table 10.2 below. The table presents assumed rankings of employer preferences, whereby the first position shows the assumed genuine preference (first-order preference) of employers and the other positions (2 to 4) show strategic preferences (lower-order preferences).

Table 10.2 Employer Preference Rankings

Employer preference rankings	
Cross-class coalition thesis (Economic interests)	Political accommodation thesis (Political interests)
1. Conservative social policies	1. No social policies
2. Liberal social policies	2. Conservative social policies
3. Social democratic social policies	3. Liberal social policies
	4. Social democratic social policies

It may be argued that the importance of work incentives for motivating employers to support conservative social policies disconfirms the political accommodation thesis. Employers' interest in work incentives is rooted in genuine economic requirements of industrial production, and independent of the political context. It is thus an objective economic interest. However, its translation into a preference for conservative social policies, I argue, was shaped by the political context. An absence of social policy is the best way of securing work incentives, conservative social policy the second-best way. Conservative social policies constituted a lesser evil, less evil than liberal and social democratic policies.

This claim is supported by empirical observations and by theoretical considerations. First, several empirical observations are consistent with the claim that conservative social policies represented a lesser evil to employers. It is remarkable that, with the exception of work injury insurance, employers have not actively promoted the formation and expansion of conservative social policies. Instead, they tended to take stances only after other actors have brought social policy issues on the political agenda. Employers have thus, in general, consented to, but not actively pushed for social policies. This is also acknowledged by scholars relying on the cross-class alliance thesis: Isabela Mares, in particular, states that "[e]mployers were not 'agenda setters'. They were not responsible for introducing a social policy proposal on the broad agenda of reform" (Mares 2003a: 259). Taking this observation seriously, one can infer that employers did not hold a first-order preference for conservative social policies, because if they would have, they would have brought such policies on the agenda on their own initiative, rather than waiting for others to take the initiative.

Second, the importance of work incentives is indicated by comparing conservative with liberal social policies with respect to labor costs. Conservative social policies will, in general, be more costly than liberal social policies, because they rely on earnings-related benefits, rather than on means-tested benefits. Employers have, however, in general preferred the earnings-related programmes of social insurance to means tested assistance programmes, which would have been likely to be less costly. This indicates that labor costs were not the only relevant issue to employers. Instead, the issue of work incentives trumped over the issue of labor costs.

Third, interests in work incentives do not provide a plausible theoretical basis for arguing that employers held a first-order preference for conservative social policies. The two theoretical arguments (see table 10.2) concur that employers will prefer conservative social

policies to liberal and social democratic ones¹⁶¹ (see table 10.2 above). This assumption is based also on robust empirical findings and, I believe, is compatible with both arguments. However, in order to show that employers' acceptance of conservative social policies reflected their first-order preference and not a second-order preference motivated by political accommodation, we would need a theoretical justification for why employers should have preferred *conservative social policy* to *no social policy* (the assumed first-order preference in the political accommodation thesis).

Employers' interest in work incentives is, however, better served by the absence of social policy than by conservative social policy. As mentioned, employers' support for conservative social policies resulted from the fact that they assumed that such policies would have less detrimental effects on work incentives compared to the two other types of social policy. Conservative social policies are less decommodifying than the two other types of social policy, because they tie benefits to previous earnings. As the existence of work incentives derives to a large extent from the fact that the worker would not be able to make a living without work, social policies, conservative or other, do necessarily reduce work incentives. In the absence of any social policy (conservative or other), employers would thus have no reason to worry about the issue of work incentives. The issue of work incentives becomes relevant to employers only once the existence of some form of social protection threatens to reduce labor supply (and thereby also to strengthen the bargaining power of unions and to push up the price of labor). In the absence of any type of social policy, there is thus no reason for employers to support conservative social policy.

In addition, one has to take into consideration that employers can also rely on occupational social benefits, instead of public social policies, to promote desired behavior among workers, such as higher work effort, loyalty and skill investments. In the absence of political constraints, occupational social benefits, sponsored by the firm itself, are likely to be the first-order preference of employers to satisfy their needs for a motivated and productive workforce. There is, therefore, a solid theoretical basis for assuming that work incentives were secondary to social pacification and political accommodation as the principle reasons for employers' acceptance of the introduction of welfare state and industrial relations institutions.

The distinction made here between (a) the motivations of employers for accepting the introduction of social policies and (b) their reasons for them preferring certain social policy

¹⁶¹ This result that employers preferred conservative social policies to other types is in line with the results presented by Mares: "The peak associations dominated by large firms have supported either private-type or contributor insurance policies. These associations have favoured these policies over alternative means-tested or universalistic social policies." (Mares 2003a: 252)

options over others demonstrates the difference between the cross-class coalition thesis and the political accommodation thesis. The cross-class coalition thesis focuses on explaining b and does so by reference to economic interests, implicitly suggesting that b also explains a. In contrast, the political accommodation thesis contends that political interests explain a, while economic interests come to play a role only in explaining b.

The introduction of work injury insurance provides a useful illustration of this distinction (see chapter 3.II). In the policy-making process, the heavy industry pushed for the inclusion in the new programme of as many sectors as possible. This stance was motivated by a preference for widening the risk pool, and for redistributing the costs across sectors. As the heavy industry was among the sectors with the highest incidence of work injuries, it thus had a clear economic interest in extending the risk pool, as argued convincingly also by Mares¹⁶² (Mares 2003a: 105). However, this observation tells us little about why the heavy industry decided to support the introduction of work injury insurance as such. In the absence of a programme for injury compensation there would have been no reason for the heavy industry to think about the whole issue of injury compensation.

As shown in chapter 3, the main reason why employers supported the programme was that the pre-existing liability legislation had turned work injuries into a source of class conflicts, fuelling class antagonizing propaganda by the unions. While different sectors may have held different preferences concerning the issue of risk pooling, this issue is logically secondary to the issue of whether a compensation programme shall be introduced at all or not. To know why employers preferred a specific option concerning the financing of the new policy tells us little about why they supported, or accepted, the policy as such. To understand the latter we need to look at the political constraints.

10. VI The VoC Thesis: Production Strategies and Preference Changes

A specific argument concerning the continued viability of welfare state and industrial relations institutions has been put forward by some proponents of the Varieties of Capitalism (VoC) perspective (2001). This argument constitutes a modified version of the cross-class coalition thesis, and I call it the “VoC thesis”. In, short, the VoC thesis suggests that, while institutions benefiting employers today may originally not have been designed or promoted by them, firms have over time managed to make positive use of these policies and, thereby, have

¹⁶² Mares argues that „employers’ concerns centred around the distribution of responsibilities in the administration of social insurance and the ‘redistribution of risks’ across different occupations” (Mares 2003a: 105)

developed also a genuine preference for their continuation (Hall and Soskice 2001: 58; Hancké et al. 2007: 20-3; Hassel 2007: 253-5; Thelen 2001: 70-76; Wood 2001: 376-9). This argument is aptly summarized by Anke Hassel:

The institutional settlement and firms' competitive strategies are ... complementary: institutions give incentives to firms to follow certain business strategies. The resulting practice by firms leads to investments that are dependent on the capacity that derives from the institutions. This, in turn, gives firms an interest in the maintenance of these institutions. (Hassel 2007: 254)

In the VoC thesis, economic interests come in not as a cause but as a consequence of the institutional setting, and are expected to contribute to a process of institutional self-reinforcement. According to the VoC thesis, the accommodation of firms to their institutional environment may give rise also to cross-class coalitions in defense of these institutions. In this perspective, cross-class coalitions serve thus not as an explanation of institutional origins, but as an explanation of the sustainability over time. Rhodes, Hancké and Thatcher, for instance, argue that

[c]ross-class coalitions in CMEs can be understood as the point where the strategies of labor and capital meet: both have strong preferences for thick, inclusive and well-institutionalised frameworks. Because both benefit, they will therefore fight for their survival. (Hancké et al. 2007: 20).

In principle, the VoC thesis is compatible with both of the two arguments that this thesis has dealt with: the cross-class coalition thesis and the political accommodation thesis, as it relates to a different temporal stage in institutional development. The cross-class coalition thesis and the political accommodation thesis are concerned with institutional origins, the VoC thesis is concerned with the subsequent adjustment of firms to the extant institutional framework. As shown in the introduction chapter, some proponents of the VoC approach endorse the political accommodation thesis on institutional origins (e.g. Hall and Thelen 2009: 14), while others argue in favor of an economic-functionalist explanation of institutional origins (e.g. Cusack et al. 2007: 388). In terms of its theoretical logic, though, the VoC thesis rests on an economic-functionalist perspective, rather than a political strategic one. Supporting the VoC thesis, Hall and Thelen, for instance, argue that "the support that groups provide for an institution is motivated, to some extent, by the benefits the institutions provides, flowing from the functions it performs" (Hall and Thelen 2009: 14).

This thesis has dealt with the VoC argument only at the margins. This is because the question that the thesis tried to answer concerned the role of employers in the historical formation of welfare state and industrial relations institutions. Therefore, the focus of the analysis was put on those historical moments when those policies and institutions that later came to define the German model were created. A systematic analysis of how German

employers subsequently accommodated their production strategies to various institutions and how this changed their perception of their interests would, for this reason, have been beyond the scope of the thesis. Nevertheless, some tentative statements on that issue are possible on the basis of the empirical analysis presented in this thesis, in particular in chapter 9, which analyzed changes in employer positions in industrial relations and welfare state reform during the 1990s.

Empirically, the evidence concerning the VoC thesis appears to be mixed. Some policies tend to confirm the development of more positive employer positions in response to their ability to use existing institutions in their own interests, others tend to disconfirm it. Moreover, we see changes in employer preferences in both directions, becoming more as well as less favorable towards existing institutions, depending on the historical period that we look at. The following paragraphs give a brief summary about the development of employer positions on the welfare state and industrial relations institutions analyzed in this thesis.

Works councils. The case of works councils confirms the VoC thesis. The importance of works councils in facilitating industrial restructuring in recent decades has been analyzed in depth by Kathleen Thelen (1991). Thelen's work indicates that works councils provided economic benefits to German firms, in particular by contributing to cooperative workplace relations and better communication between management and workforce. Today, German industry generally supports works councils and acknowledges their positive effects in terms of social peace and cooperative workplace relations.¹⁶³

Initially, though, industry had been adamantly opposed to the institutionalization of works councils. Mandatory Works councils were first introduced during World War I, as part of the Auxiliary Services Act of 1916, a decision intended by the government to pacify a discontent working class. At that time, industrial employers accepted mandatory works councils only as a temporary institution limited to the period of the war. After World War I, however, industrialists changed their position and accepted the permanent establishment of mandatory works councils in return for the unions' cooperation against revolutionary forces (see chapter 4). After the revolutionary threat had waned, employers revoked their concession and opposed the passing of the Works Councils Law in 1919. Employers suspected that the works councils would provide a hotbed of radical union agitation.

¹⁶³ The share of workers covered by works councils did, however, went down somewhat in recent years, from 50 per cent in 1996 to 46 per cent in 2005 (Ellguth 2007: 157).

The practical experiences with works councils made by German firms during the Weimar Republic appear to have been mixed. While some firms refused to establish works councils, despite the legal requirement to do so, other firms reported positive experiences with their works councils (Erdmann 1966b: 145). After World War II, works councils became generally accepted and endorsed by industrial employers. In the 1950s, the employer federation (BDA) advocated works councils as a strategic alternative to co-determination in the supervisory board, but later on support for works councils came to rest also on a genuine belief that they constitute an expedient tool to facilitate communication between management and workforce (see e.g. Balke 1966: 6).

Collective bargaining. Sectoral wage bargaining provides a good case for testing the VoC thesis, because bargaining coverage rests on voluntary membership by firms. Sectoral wage bargaining is thus not a mandatory institution and participation by firms in wage bargaining can be seen as indicating genuine support. In the Wilhelmine Empire (1871-1918), most sectors had refused to recognize unions and to bargain with them.¹⁶⁴ They tried to undermine unions by repressive means, such as blacklisting (see chapter 2.II). Some small-firm sectors started to bargain with unions from about the turn of the century on, most notably construction and timber, but the large heavy industry sector continued to refuse to recognize labor unions. Sectoral bargaining was extended to all sectors in 1918 by the Stinnes-Legien agreement, covering now also those sectors that until then had refused to even recognize unions. Collective bargaining institutions remained contested by employers throughout the Weimar Republic, in particular the role of binding state arbitration in settling wage conflicts. Wage bargaining in the Weimar Republic was conflictual and often resulted in an impasse that had to be solved by state intervention.

Like in the case of works councils, employers changed their attitude towards collective bargaining after World War II, a change that was part of their broader paradigm shift towards social partnership and social compromise (see chapter 6). Industrial employers came to see sectoral bargaining as a tool expedient for securing social peace and keeping wage conflicts away from the workplace (see e.g. Müller-Jentsch 1993: 496-7). Collective bargaining became thus genuinely supported by employers. Starting in the mid-1980s, though, bargaining coverage declined considerably due to individual firms deciding to leave sectoral bargaining (see chapter 9.IV). This trend is caused in particular by the exit of smaller firms, which increasingly find collective agreements as too burdensome and too costly. Large firms do in

¹⁶⁴ An exception to this was the printing sector, where collective bargaining occurred already from the 1870s onwards (see chapter 2). The example of the printing sector was however initially not followed by other sectors.

general tend to stay within the sectoral bargaining institutions. They tend to perceive sectoral bargaining as providing genuine economic advantages, most importantly in terms of securing social peace and facilitating the peaceful restructuring of production. The exit by smaller firms has resulted in a significant shrinking of the German model in terms of the share of the economy it covers. With respect to collective bargaining, evidence for the VoC thesis thus tends to concentrate on the post-war period. The more recent period, since the mid-1980s, shows a more ambivalent attitude by employers, characterized by the emergence of internal differences that remained muted in the post-war period. We will return to this issue further below.

Codetermination. As shown in chapter 8, employers opposed the introduction and extension of codetermination at the firm-level (i.e. power-sharing in supervisory boards) in the post-war period, though they did over time come to accept it. Up to the 1970s, employers campaigned fiercely against parity representation in the supervisory board, and in particular against the extension of its coverage by the Codetermination Law of 1976. After they had failed to bring down the law through a constitutional complaint in 1977, employers decided to put up with codetermination and since then toned down their campaigning against codetermination. They continue to push for restricting codetermination rights and argue that codetermination constitutes a competitive disadvantage for attracting investors on international financial markets (BDI and BDA 2006; Kommission zur Modernisierung der deutschen Unternehmensmitbestimmung 2006: 55-66). In contrast, the more limited form of codetermination established by the Workplace Constitution Law of 1952 and applied in smaller firms (“one-third codetermination”) is generally accepted by employers today. The decision by employers to put up with parity codetermination appears to be largely the result of political accommodation, rather than of the perception of genuine economic benefits.

Welfare state programmes. The social policy field provides mixed evidence for the VoC thesis. Throughout most of history the focus of employers was to limit welfare state expansion (*politics of containment*), rather than to defend existing policies against retrenchment. In the 1880s, employers supported Bismarck’s reforms as an instrument for the social pacification of a discontent and politically radicalized working class. Later, the waning of revolutionary fears and the sustained rise in social expenditures resulted in a shift in employers’ attitudes. Arresting the further expansion of the welfare state became the paramount goal of employers. To achieve this goal they often acted strategically and presented alternative policy proposals.

From the 1990s onwards, employers greatly intensified their calls for welfare state retrenchment and cost containment. At the same time, they moved away from political accommodation and social compromise, as shown in chapter nine. They intensified public campaigning for welfare state retrenchment and market-oriented reforms and began to take more radical policy positions. This constitutes a significant change compared to previous decades, when employers did in principle accept the German model of consensual policy-making. During the post-war period two types of interests underpinned employers' acceptance of the basic institutional elements of the German welfare state: The role of social policies in industrial restructuring, and organizational self-interests of the employer associations themselves.

The role of social policy for peaceful industrial restructuring

From the 1970s onwards, firms often made use of social policy programmes to facilitate peaceful labor shedding, when the structural decline of the heavy industry and the restructuring of production in other sectors made large-scale lay-offs unavoidable. They made use of programmes like unemployment insurance, disability pensions or other provisions for early exit from the labor market to shed older workers (see e.g. Jacobs et al. 1991: 198-205). This practice provided them with a genuine economic interest in certain social policy programmes, as they allowed firms to reduce and restructure their labor force, while at the same time maintain social peace and cooperative relations with their workforce (see e.g. Ebbinghaus 2006: 43-49). Over time, however, the resulting rise in non-wage labor costs came to outweigh the advantages of this practice to firms. From about the mid-1990s onwards, employers became increasingly critical towards this practice of labor shedding-cum-social pacification. Today, the national employer federation officially demands a systematic closing down of possibilities for early retirement (BDA 2009: 19). The congruence of employer interests and generous social policy provisions appears thus as a temporary phenomenon, as characteristic for a specific historical phase that seems to be coming to an end.

With some simplification, we can interpret the general pattern that emerges from the four sectoral trajectories above as a U-shaped curve. During the post-war period employers developed genuine preferences for certain aspects of welfare state and industrial relations institutions whose formation they had originally opposed. More recently, especially since the 1990s, we see a backlash, a turn away by employers from certain policies and institutions they accepted or endorsed during the post-war decades. The employer associations turned against early retirement provisions, even though many firms did in the past make extensive use of

such provisions. They turned away from consensual policy-making and towards public campaigning and opinion formation. Moreover, smaller firms tended to abandon collective bargaining, a process which the associations did not try to stop and, in effect, even supported by creating bargaining opt-outs for their members (“OT memberships”).

Organizational interests in corporatist governance

While employers today campaign strongly for welfare state retrenchment, including the closing down of programmes for early retirement, they continue to defend the corporatist governance of social policies, known in Germany as “parity self-government” (BDA 2008: 2-3). Already during the Weimar Republic, employers consistently supported corporatist forms of social policy administration, instead of unilateral administration by the governmental bureaucracy. They pushed for the corporatist administration of unemployment insurance in the 1920s and for the re-instatement of corporatist administration after World War II (see sections 5.II and 7.II). As pointed out by Philip Manow, their participation in corporatist social policy administration contributed to the formation of cooperative and trust-based relations between unions and employer associations (Manow 2001: 119-20), and thereby also to the institutional underpinnings of social compromise in the post-war period.

In addition to facilitating cooperative relations with unions, the employer associations also have a strong organizational self-interest in corporatist governance. Their participation in social policy administration provides unions and employer associations with organizational legitimacy and resources. It strengthens their standing in politics and helps them to justify a large staff vis-à-vis their members. While the employer associations defend their role in corporatist governance on the grounds that thereby they can ensure the efficient use of social insurance funds, and thereby help to prevent higher labor costs, their scope to influence social expenditure levels is in reality extremely limited, as benefit entitlements are determined entirely by the legislator, with virtually no discretion for the administration (Trampusch 2006: 347-8). The reasons for employers’ support for corporatist “self-government” are, thus, to a large extent rooted in the organizational interests of their associations, rather than in the economic interests of individual firms.

Internal conflicts and interest aggregation

The turn by employer associations towards more radical and less accommodating stances is to a considerable extent fuelled by the emergence of internal conflicts, conflicts that had been largely muted during the post-war period. As we have seen in the introductory chapter

(section 1.II), the social policy interests of different types of firms are aggregated by the national employer federation (BDA), which formulates a common standpoint, taking into account also strategic considerations. Because of this, internal differences within the business community do not normally come to have an impact in the field of welfare state politics. A specific division of labor among business interest associations, characteristic for corporatist systems of interest representation, serves to mute interest pluralism. This division of labor has two dimensions:

First, business interest associations divide up responsibility for policy fields among each other, and tend not to compete with each other in defining policy positions. As a result, the national employer federation BDA enjoys a near-monopoly position in formulating and representing the social policy positions of industrial firms in national politics. It represents the social policy interests of its members vis-à-vis the government, the legislature, other political actors and the public in general. Other peak-level business federations have an equivalent role in representing the product market interests of firms (BDI, DIHT and ZDH). These federations tend not to have their own positions on social policy issues, but do instead tend to back the BDA's social policy positions. Their social policy statements tend to be of a very general nature and are intended mainly to add strength to the BDA and its stances, rather than to compete with the latter.

Second, a clear division of labor between peak-level and sector-level employer associations contributes to muting internal differences. The main task of sector-level employer associations is to bargain with unions. They do not normally engage a lot in welfare state politics. Instead, as mentioned above, the political representation of employers' social policy interests is done by their peak-level federation, the BDA (see e.g. Grote et al. 2007: 160-2). While the BDA enjoys a *de facto* monopoly in representing the social policy interests of industrial employers, this does not necessarily mean that its positions are always representative for the business community at large, but potential dissenters are weakly organized and have no strong means to make their voice heard in national politics.¹⁶⁵ This holds in particular for conflicts between small and large firms, which have surfaced during the 1990s, in particular on the issue of early retirement and in collective bargaining. Big industry dominates decision-making within the BDA, as membership fees and voting rights are linked to firm size. At the same time, smaller firms do not command strong independent

¹⁶⁵ An example of a dissenting group is the ASU ("*Working Group of Independent Entrepreneurs*"). The ASU represents smaller, family-run enterprises and pursues an unabashedly neo-liberal line. The ASU sees the welfare state as Germany's main competitive disadvantage and calls for a privatization of welfare state programs (ASU 2005: 32). Even today, the ASU presents codetermination in its various forms as a disguised form of socialism and as an unacceptable infringement on private property rights (ASU 2006: 1).

organizational means for representing their positions. As a result, intra-business conflicts are played out predominantly within the associations and do usually not surface in the making of public policies.

Internal conflicts between small and large firms have pushed the employer associations to radicalize their positions during the 1990s, though. In the past, the existence of a common opponent, such as a reformist government or the labor movement, often united the employer side and helped the associations to contain internal conflicts where they existed. Warding off revolutionary or reformist threats had priority over internal differences over policy details. During the 1990s the associations' ability to contain internal conflicts declined as a result of increasing dissatisfaction among smaller firms in several fields. This required the associations to pay closer attention to the preferences of their smaller members and limited their capacity to accept political compromises. Thus, using the conceptual terms offered by Schmitter and Streeck, they had to shift from a "logic of influence" to a "logic of membership" (Schmitter and Streeck 1981).

In the field of collective bargaining, differential capacities to deal with intensified competitive pressures and rising non-wage labor costs resulted in conflicts between small and large firms. Large firms tried to deal with competitive pressures and the need for industrial restructuring by pushing for decentralizing and flexibilising arrangements within collective agreements. Smaller firms tended to leave collective bargaining institutions entirely, because they had fewer opportunities to make use of flexibilising arrangements, and came to see collective agreements increasingly as a burden, rather than as a contribution to social peace. As a result, collective bargaining coverage eroded considerably (see chart 9.2). In response, the associations decided to allow members to opt-out from collective bargaining, which contributed further to the erosion of collective bargaining institutions. Some employer associations in eastern Germany even actively encouraged their members to leave collective bargaining (VSME 2007). Similarly, the BDA's turn against early retirement is a response to intensified dissatisfaction among smaller firms, as early retirement was primarily used by larger firms. In short, while larger firms may still remain comparatively content with existing institutions, the official stances of employer associations became increasingly shaped by the concerns of smaller firms, contributing to their turn towards market liberalization and welfare retrenchment.

The continued relevance of strategic accommodation

Event though a radicalization of employer positions took place during the 1990s, strategic accommodation continues to play an important role even today. In specific reform processes, employer associations often decide to put forward rather moderate proposals in order to increase their chances of making an impact. Employer associations rely on good contacts with government officials to make their voice heard and try to cultivate these contacts by putting forward politically and technically feasible reform proposals. As shown in chapter 9, also today the BDA's reform proposals are pitched towards the politically feasible, while at the same time aiming for considerable cost reductions. Like in the past, this moderation of positions reflects strategic considerations. For instance, the shift by the BDI towards a more unabashedly neo-liberal stance in the 1990s was contested within industry because of fears that this would undermine industry's political credibility and influence. Moreover, the inability of capital and labor to reach a compromise in the *Alliance for Jobs* talks indicates that employers are not content with small-scale, incremental reforms but want far-reaching reforms, pushing for labor market liberalization and welfare state retrenchment.

The funding by employers of public campaigns that promote market-liberalizing reforms, such as the INSM, supports the view that their moderation of official positions on social policy issues reflects strategic considerations, rather than a genuine economic preference. Since the early 1990s, the continued rise in non-wage labor costs, and the slow progress of cost containing reform, made employers increasingly critical of the effectiveness of political accommodation as a political strategy. Employers came to identify public opinion as a major obstacle for the reforms they desired. Political accommodation helped employers to influence the decisions of elite policy-makers, but it did, at the same time, also limit their ability to influence public opinion.

As long as political accommodation worked reasonably well for them, they did not consider this as a major problem and had no particular urge to shape public opinion. In particular from the 1980s onwards, however, political accommodation became less effective, because the reasons for the rise in non-wage labor costs shifted from deliberate political decisions to expand social policies to structural causes, like higher unemployment and demographic ageing. These structural causes were difficult to combat by way of political accommodation and compromise, and required employers to make more forceful political interventions instead. The desired structural reforms of the welfare state required employers to try to coax government into making far-reaching, but unpopular, decisions. In the context of fiscal austerity, employers now had to convince governments to make more far-reaching

reform efforts, in order to reduce labor costs, rather than to contain reform efforts, as in the post-war period of welfare state expansion. Towards this end, public campaigning appeared more effective than political compromise. Through public campaigning they tried to change public opinion on broad political issues concerning the role of the state and markets in society, and thereby to weaken electoral resistance against market-liberalizing reforms.

To conclude, the empirical development confirms the VoC thesis in parts, but disconfirms it in other parts, depending on the historical time frame we focus on. The historical pattern approximates roughly a U-shaped curve. Developments in the post-war period tend to be broadly in line with what the VoC thesis predicts, as employers did over time become genuinely supportive of institutions and policies they had initially either opposed, or accepted only as lesser evils. This holds in particular for collective bargaining and the works councils. This development appears to have been in part the result of a genuine change in economic preferences, rather than only a strategic adjustment to political constraints, like what was the case in the preceding political regimes.

Developments in the more recent period tend to disconfirm the VoC thesis, however. Employers have become a driving force for liberalizing reforms, rather than defenders of the *status quo*. This is most evident in the erosion of collective bargaining institutions and in public campaigning for labor market liberalization and welfare state retrenchment. As argued in chapter nine, this second shift in employer positions appears to be explained by a combination of endogenous problems created by existing institutions, most importantly the unrelenting rise in non-wage labor costs, and the intensification of cost competition due to globalization. In addition, internal differences between large and small firms, with the latter being under greater competitive pressures, have further fuelled the radicalization of employer positions. This second shift suggests that, while firms may try to adjust their production strategies to existing institutional constraints, and to the extent that they succeed in doing so also develop more favorable preferences, their actual capacity to do so successfully may be eroding. During the post-war period, the adjustment of production strategies and high levels of economic growth allowed employers to reconcile political accommodation and economic competitiveness, and thereby to safeguard social peace. Over time, however, the sustained rise in non-wage labor costs eroded employers' capacity to reconcile their own economic interests with political accommodation.

Conclusions

To conclude, this thesis has put forward the argument that German employers accepted the formation of social policies and industrial relations institutions as a lesser evil. German employers have consistently tried to shape social policies in line with their preferences, but what they wanted was decisively shaped by the political context. Their acceptance of the introduction of social policies and institutions of social compromise did not reflect any objective economic necessities of profit-seeking firms, but resulted from political constraints that shaped what employers thought would be the policies worth fighting for. Politically generated challenges, the “*greater evils*,” compelled employers to put their weight behind policies that otherwise would have been of no value to them.

The nature of the greater evils employers wanted to prevent changed over time and so did the lesser evils that they thought would be most effective in fighting the first. Originally, fears of a social revolution, the collectivization of industry and loss of political power, constituted the greater evils that employers tried to fight off. The pacification of the working class, or politically radicalized segments within it, constituted the means for doing so. Thereby, employers reluctantly came to accept those same social policies and institutions of class cooperation that they had previously opposed. With the waning of revolutionary dangers and the reformist transformation of the labor movement also the kinds of challenges faced by business shifted. Now, universalistic policies that were seen as undermining work incentives and welfare state expansion became the new “greater evils.” Strategically motivated and more moderate alternative proposals were the lesser evils. In short, the formation of the modern welfare state may not have been fundamentally opposed by capitalists, but it is unlikely that they would have accepted it in the absence of strong pro-welfare forces.

Appendix: Time Line

1869	Deutscher Buchrdruckerverein founded (first permanent national employer association)
1871	Freedom of association enshrined by law
1872	<i>Verein für Socialpolitik</i> founded
1873	<i>Association of German Iron and Steel Industrialists</i> (VDESI) founded
1876	<i>Central Association of German Industrialists</i> (CDI) founded as the first national industry federation
1875	German Social Democratic Party founded
1878	anti-socialist legislation enacted
1878	Verein anhaltischer Arbeitgeberverbände founded by Oechelshäuser
1879	protectionist tariffs policy introduced
1881	'Social peace message' by Emperor Wilhelm I. announces plans to introduce social insurance
1883	national health insurance law passed
1884	national work injury insurance law passed
1889	old-age and disability pensions law passed
1890	anti-socialist legislation discontinued
1890	<i>Gesamtverband Deutscher Metallindustrieller</i> founded (nationwide metal employer federation)
1895	<i>Bund der Industrie</i> (Federation of Industry) founded
1901	<i>Verein für Sozialreform</i> founded
1903/04	Large strike by textile workers in <i>Crimmitschau</i>
1904	first national peak-level employer federations founded (<i>Hauptstelle</i> and <i>Verein</i>)
1909	<i>Hansabund</i> founded, as a political business organization
1910	Large strike by construction workers
1913	merger of <i>Hauptstelle</i> and <i>Verein</i> into VDA (Association of German Employer Associations)
1914	Begin of World War I
1916	War Auxiliary Services Law (HDG) passed (participatory rights to unions)
1918	November: end of World War I, November Revolution, Stinnes-Legien Agreement
1919	winter 1918/19 large strikes in mining
1919	Weimar Republic founded
1919	<i>BdI</i> and <i>CDI</i> merge into <i>RDI</i> (Federation of German Industry)

1920	January: Works councils law passed
1920	June: Central Committee (Zentralausschuss) of German Business Associations founded
1920	Kapp-Putsch (attempted <i>putsch</i> by right-wing paramilitaries)
1924	Ruhr occupation by French and Belgian troops
1924	employers unilaterally abandon the agreement on the eight hour working day
1924	collapse of the ZAG
1924	Ernst von Borsig new VDA president (until 1932)
1927	Unemployment Insurance Law (AVAVG law) introduced
1929	'Ruhr iron conflict' (largest industrial conflict during the Weimar period)
1929	outbreak of the world economic crisis
1930	government Müller-Franken resigns over unemployment insurance conflict
1932	Carl Köttgen new BDA president (until 1933)
1933	Nazis come into power: unions and employer associations banned. Formation of the <i>Deutsche Arbeitsfront (DAF)</i> as a joint organization for capital and labor
1936	Formation of the <i>Reichswirtschaftskammer</i> [national economic chamber] by the Nazis
1939	Begin of World War II
1945	End of World War II, defeat of the Nazi regime, begin of Allied occupation
1949	currency reform
1948	June: formation of a national committee of employer associations
1950	Social Insurance Adjustment Law passed by the Economic Council
1949	Constitution of the new Federal Republic passed
1949	August: First national elections, formation of a CDU-led government (Chancellor: Konrad Adenauer, in power until 1963)
1949	October: formation of a national, non-partisan, union federation (DGB)
1951	BDA (Federation of German Employer Associations) founded. First BDA president: Raymound (until 1953)
1950	January: Hattenheim talks between capital and labor over co-determination conflict
1950	October: Law re the re-establishment of self-government in social insurance passed
1951	May: Co-determination Law for the heavy industry passed (Montan Codetermination Law)
1951	August: Dismissal Protection Law
1952	November: Workplace Constitution Law passed
1953	Hans Constantin Paulssen new president of the BDA (until 1964)
1957	pension reform introducing wage indexation ("dynamic pension") passed
1961	Construction of the Berlin Wall
1963	new CDU-led government (until 1966, chancellor: Ludwig Erhard)

1963	Council of Economic Experts (Sachverständigenrat) established
1964	Siegfried Balke new BDA president (until 1969)
1964	Chancellor Erhard initiates expert group for social policy reform ('Sozial-Enquete')
1966	Grand Coalition between SPD and CDU (Chancellor: Kurt Kiesinger, until 1969)
1967	Start of the <i>Concerted Action</i> talks (tripartite body on macro-economic policy concertation), until 1977
1967	<i>Biedenkopf commission</i> on reform of codetermination established (reports 1970)
1969	Otto Friedrich new BDA president (until 1973)
1969	Social-liberal coalition (until 1982, Chancellors: Willy Brandt, followed by Helmut Schmidt)
1972	Reform of the Works Constitution Law (extends works councils rights)
1973	Hans-Martin Schleyer new BDA president (until 1977)
1976	Special Codetermination Law (extends codetermination rights in large firms), employers file a constitutional complaint against the law
1977	July: unions leave Concerted Action talks in protest against employers challenging the 1976 codetermination law in court
1977	October: BDA president Schleyer assassinated by RAF
1978	Otto Esser: new BDA president (until 1986)
1979	Federal Constitutional Court confirms constitutionality of parity codetermination
1982	CDU-led (conservative-liberal) coalition (until 1998, Chancellor: Helmut Kohl)
1984	large strikes in metalworking on the issue of a shorter working week, results in a flexibilisation of working time rules and a gradual reduction of weekly working time
1986	Klaus Murmann new BDA president (until 1996)
1989	November: Berlin Wall falls
1990	German unification: March 9th: joint declaration by BDA and DGB on the extension of the West German industrial relations model to the East and a policy of rapid wage convergence October 3rd: Reunification
1991	First wage convergence agreements signed in many sectors
1993	February: Metal employers unilaterally cancel wage convergence agreements,
1994	Introduction of long-term care insurance against the resistance of employers
1996	Dieter Hundt new BDA president
1998	red-green coalition (until 2005, Chancellor: Gerhard Schröder)
2002	Hartz committee on labor market policy reforms (several reform measures later implemented)

2005	Grand Coalition between CDU and SPD (Chancellor: Angela Merkel)
2006	Expert Commission on the reform of codetermination.

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